AIDING AMERICAN BUSINESSES ABROAD: GOVERNMENT ACTION TO HELP BELEAGUERED AMERICAN FIRMS AND INVESTORS

HEARING

BEFORE THE

SUBCOMMITTEE ON TERRORISM, NONPROLIFERATION, AND TRADE

OF THE

COMMITTEE ON FOREIGN AFFAIRS
HOUSE OF REPRESENTATIVES

ONE HUNDRED TENTH CONGRESS

SECOND SESSION

JULY 17, 2008

Serial No. 110–222

Printed for the use of the Committee on Foreign Affairs

Available via the World Wide Web: http://www.foreignaffairs.house.gov/

U.S. GOVERNMENT PRINTING OFFICE
43–521PDF WASHINGTON : 2008

For sale by the Superintendent of Documents, U.S. Government Printing Office
Internet: bookstore.gpo.gov Phone: toll free (866) 512–1800; DC area (202) 512–1800
Fax: (202) 512–2104 Mail: Stop IDCC, Washington, DC 20402–0001

COMMITTEE ON FOREIGN AFFAIRS

HOWARD L. BERMAN, California, *Chairman*

GARY L. ACKERMAN, New York
ENI F.H. FALEOMAVAEGA, American Samoa
DONALD M. PAYNE, New Jersey
BRAD SHERMAN, California
ROBERT WEXLER, Florida
ELIOT L. ENGEL, New York
BILL DELAHUNT, Massachusetts
GREGORY W. MEEKS, New York
DIANE E. WATSON, California
ADAM SMITH, Washington
RUSS CARNAHAN, Missouri
JOHN S. TANNER, Tennessee
GENE GREEN, Texas
LYNN C. WOOLSEY, California
SHEILA JACKSON LEE, Texas
RUBÉN HINOJOSA, Texas
JOSEPH CROWLEY, New York
DAVID WU, Oregon
BRAD MILLER, North Carolina
LINDA T. SÁNCHEZ, California
DAVID SCOTT, Georgia
JIM COSTA, California
ALBIO SIRES, New Jersey
GABRIELLE GIFFORDS, Arizona
RON KLEIN, Florida
BARBARA LEE, California

ILEANA ROS-LEHTINEN, Florida
CHRISTOPHER H. SMITH, New Jersey
DAN BURTON, Indiana
ELTON GALLEGLY, California
DANA ROHRABACHER, California
DONALD A. MANZULLO, Illinois
EDWARD R. ROYCE, California
STEVE CHABOT, Ohio
THOMAS G. TANCREDO, Colorado
RON PAUL, Texas
JEFF FLAKE, Arizona
MIKE PENCE, Indiana
JOE WILSON, South Carolina
JOHN BOOZMAN, Arkansas
J. GRESHAM BARRETT, South Carolina
CONNIE MACK, Florida
JEFF FORTENBERRY, Nebraska
MICHAEL T. MCCAUL, Texas
TED POE, Texas
BOB INGLIS, South Carolina
LUIS G. FORTUÑO, Puerto Rico
GUS BILIRAKIS, Florida
VACANT

ROBERT R. KING, *Staff Director*
YLEEM POBLETE, *Republican Staff Director*

SUBCOMMITTEE ON TERRORISM, NONPROLIFERATION, AND TRADE

BRAD SHERMAN, California, *Chairman*

DAVID WU, Oregon
DAVID SCOTT, Georgia, *Vice Chair*
RON KLEIN, Florida
GENE GREEN, Texas
JOSEPH CROWLEY, New York

EDWARD R. ROYCE, California
JOHN BOOZMAN, Arkansas
TED POE, Texas
DONALD A. MANZULLO, Illinois
THOMAS G. TANCREDO, Colorado

DON MACDONALD, *Subcommittee Staff Director*
JOHN BRODTKE, *Subcommittee Professional Staff Member*
TOM SHEEHY, *Republican Professional Staff Member*

CONTENTS

AIDING AMERICAN BUSINESSES ABROAD: GOVERNMENT ACTION TO HELP BELEAGUERED AMERICAN FIRMS AND INVESTORS

THURSDAY, JULY 17, 2008

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON TERRORISM, NONPROLIFERATION, AND TRADE,
COMMITTEE ON FOREIGN AFFAIRS,
Washington, DC.

The committee met, pursuant to notice, at 10:05 a.m. in room 2200, Rayburn House Office Building, Hon. Brad J. Sherman (chairman of the subcommittee) presiding.

Mr. SHERMAN. Thanks for being here. I want to commend Ranking Member Royce for suggesting these hearings. Today, we are going to examine how the U.S. Government can better aid American business and investors abroad that are involved in commercial disputes and disputes with the host government, particularly when they are not being treated fairly and according to rule of law.

It is the general policy of the United States Government that American citizens involved in commercial disputes must exhaust all local remedies before the U.S. Government will take action. We will explore whether this is a wise policy.

When given, U.S. assistance largely focuses on providing a list of attorneys who are willing to defend U.S. nationals—the Martindale Hubbell Company does this, as well—and sharing information about the legal system, and providing basic information about how to contact host government officials to address their claims.

The hearing will examine what the U.S. can do to create a more coordinated and effective process for helping beleaguered American businesses in foreign countries, especially in countries where a just and sound legal system is not necessarily available.

We will also explore what we can do to warn Americans that certain countries are not hospitable in general, because they do not have the rule of law, or in particular, to U.S. businesses; and finally, what we can do to limit access to the United States market to those companies that systemically deny us, through their abuses, access to commercial opportunities.

As we examine these issues, we must realize that corruption is a serious problem in a lot of countries—occasionally our own; perhaps even in Pasadena.

We are a country of laws, and we respect the rule of law most of the time. That is not the case everywhere. At times, the legal systems in various countries overseas do not provide the structure

that is just and sound. Even when a system provides a rule of law generally, you still face particular discrimination against the United States and its business enterprises or against what they regard as foreigners in general.

For example, the Economist Intelligence Unit asserts that judges in China continue to take directions from party and government leaders; and occasionally bribes, as well.

At the legal level in China, judges are very unlikely to rule against state-owned enterprises. In many areas, foreign-invested enterprises actually avoid taking disputes to domestic courts if they can; and even if they do, enforcement of court verdicts remains problematic.

There is, of course, the arbitration process; and we ought to examine that, particularly with reference to China. When a U.S. company runs into dispute, it naturally seeks arbitration on neutral ground. In turn, Chinese companies, especially the state-owned, are pushing for their business contracts with Western companies to stipulate that arbitration takes place in mainland China.

Of course, when you have an uneven bargaining position, when it is the policy of the United States to give China total access to our markets no matter what, and the policy of the Chinese to give access to their markets only to companies that sign unequal contracts, you may be forced into one of these one-sided arbitration agreements.

A prime example of some of the unfair practices and hostile business environments U.S. companies come into contact with was documented by Professor Jerome Cohen of NYU, who served on a Chinese arbitration panel in 2005 with, I believe, two Chinese nationals in this case.

A U.S. based power company claimed losses of $35 million. The arbitrators ruled two to one in favor of the Chinese company; and Professor Cohen asserts that the Chinese company committed the most blatant contract violations he had ever witnessed in a very long career.

So one might wonder, well, why is it that Chinese arbitrators have a tendency to go with the Chinese litigant? One case that concerned two linked disputes with PepsiCo and a Chinese bottler in which PepsiCo alleged several breaches of various contracts and sought an order terminating the joint venture.

The arbitration hearings were held in Stockholm. PepsiCo had not been forced into one of these unequal, must-arbitrate here contracts. These were first major arbitrations involving a multinational corporation and a Chinese state-owned company since China entered the WTO.

As it happened, one of the arbitrators selected was a Chinese national, Dr. Wang Shengchang, who was a Chinese national. He voted in favor of PepsiCo, showing remarkable focus on his profession. Coincidentally, a few months later, he was apprehended and has not been heard from since.

One wonders what message this sends to Chinese arbitrators in general and what message it sends to the world, when the United States does nothing about this or the other instances that will come out in these hearings; and has almost a religious dedication to keeping our market open, no matter what anybody ever does to us.

One of my deepest frustrations over many international trade agreements has been the unwillingness of our trading partners to fulfill their obligations. In one case, NAFTA—for example, Fireman's Fund, which is a large insurance company in my state of California, purchased $50 million in debt instruments from a Mexican bank in 1995.

At the same time, a similar debt instrument purchase was made by various Mexican investors. When the bank began to experience financial difficulties in 1997, the Mexican banking and financial authorities allowed the Mexican investors to redeem their notes, while denying the same treatment to Fireman's Fund. In my view, this is a blatant case of discrimination; one that our Government has responded to very inadequately.

Because it is a matter involving financial institutions, Fireman's Fund is not allowed to bring a NAFTA action. Those who sold NAFTA to us did not point that out at the time it was negotiated; and instead must rely on the U.S. Government to pursue the action.

All efforts to convince Mexican authorities of the inequities of their position have gone unanswered. The factual record strongly supports Fireman's Fund and strongly some inquiry today as to why so little has been done by the U.S. Government.

Indeed, a NAFTA tribunal which ruled on an underlying expropriation case in 2006, said the facts clearly reveal that Fireman's Fund was the victim of a severe injustice.

What is the U.S. response? I have alluded to that earlier. The scope of U.S. assistance in these cases consists chiefly of advice on how to deal with the legal system; as if the published legal system is, in fact, what happens to them.

Under limited circumstances and coordination with the Justice Department, the State Department may authorize a consular officer to appear before a foreign court or tribunal to request a suspension of a proceeding to give a U.S. citizen time to obtain legal representation, if that U.S. company had not looked at Martindale Hubbell and selected a lawyer earlier or on time.

Simply put, the government too often does not take specific action to assist U.S. companies' investors, even in situations where it is known that the legal system does not work.

As I may have mentioned earlier, Commerce's Office of Market Access and Compliance does offer U.S. businesses a Trade Complaint Hotline through its TCC on-line application for assistance on commercial disputes in host countries. However, last year, the Office of Market Access and Compliance was able to resolve half the cases.

It is said that all we need to do is provide some more resources. I would say we do need to look at three other approaches, as well. One is to advocate at the foreign ministry level. The second is to warn; to publish a list of those countries that either do not have the rule of law in general or treat Americans poorly.

We are warned, do not travel to this country to get a suntan. But nobody warns us, do not travel to this country to do business.

Finally, we have to look at intradiction or other action, so that countries that are on the warning list—which means that they are not treating us fairly—do not think that they have unimpaired ac-

cess to U.S. markets forever, no matter how they treat U.S. business.

Because, in fact, I think China might like being on the warning list, if we specified that those who try to exploit the Chinese market will not be treated fairly; those who are doing off-shoring will be treated fairly. They might actually like that notice, as long as they knew that we were too weak, too feeble, and too divided to then say if we do not have access to exploit your market, you will not have access to exploit ours.

So I look forward to a foreign policy of the United States that does something about what remains, in spite of the low dollar, the largest trade deficit in the history of the world, except for last year's U.S. trade deficit. With that, I will yield to our ranking member.

[The prepared statement of Mr. Sherman follows:]

PREPARED STATEMENT OF THE HONORABLE BRAD SHERMAN, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF CALIFORNIA, AND CHAIRMAN, SUBCOMMITTEE ON TERRORISM, NONPROLIFERATION, AND TRADE

Today's hearing is to examine how the U.S. Government can better aid American businesses and investors abroad that are involved in commercial disputes or disputes with the host government.

It is the general policy of the U.S. government that American citizens involved in commercial disputes must exhaust all local remedies before the U.S. government will take action.[1] When given, U.S. assistance largely focuses on providing a list of attorneys who are willing to defend U.S. nationals, sharing information about the legal system, and providing basic information about how to contact host government officials to address their claims.

The hearing will examine what the U.S. can do to create a more coordinated and effective process for helping beleaguered American businesses in foreign countries, especially in countries where a just and sound legal system is not necessarily available.

LEGAL SYSTEM/ CORRUPTION OVERSEAS

As we examine this issue we must realize that corruption is a serious and real problem.

We are a country of laws, and we respect the rule of law. That is not the case everywhere. At times, the legal systems in various countries overseas do not provide a structure that is just and sound, making it more difficult for companies to bring claims to the court system.

While this is certainly a legitimate concern for foreign policy makers, such corruption can be catastrophic to a U.S. exporter or investor.

For example, the Economist Intelligence Unit asserts that judges in China continue to take directions from party and government leaders—and occasionally bribes.[2]

At the local level in China, judges are very unlikely to rule against state-owned enterprises. In many areas, foreign-invested enterprises actually avoid taking disputes to domestic courts if they can, and even if they do, enforcement of court verdicts remains problematic.[3]

ARBITRATION PREFERRED TO DOMESTIC COURTS OVERSEAS

What has been the response to these charges of judicial failings in countries like China?

When a U.S. company runs into a dispute, it naturally seeks arbitration on neutral ground. In turn, Chinese companies, especially the state-owned, are pushing for

[1] CRS Report: "U.S. Government Assistance on Foreign Investment Disputes", July 9, 2008; Page # 2

[2] Country Briefing from the Economist Intelligence Unit, China Risk: Legal & regulatory risk; (May 2, 2008); www.eiu.com

[3] Country Briefing from the Economist Intelligence Unit, China Risk: Legal & regulatory risk; (May 2, 2008); www.eiu.com

their business contracts with Western companies to stipulate that conflicts go to arbitration in mainland China.

A prime example of some of the unfair practices and hostile business environments U.S. companies come into contact with overseas was well documented by Professor Jerome Cohen of NYU, who served on a Chinese arbitration panel in 2005. In this case, a U.S.-based power company claimed its Chinese joint venture partner had breached a contract to build a power plant, leading to a loss of $35 million. The arbitrators ruled 2–1 in favor of the Chinese company despite the American arbitrator's assertion that the Chinese company had committed the "most blatant contract violations" he had ever witnessed.[4]

There is also concern over how these arbitrators are paid and what kind of repercussions they face for siding with a foreign-owned company.

One case concerned two linked disputes between PepsiCo and a Chinese bottler in which PepsiCo alleged several breaches of various contracts and sought an order terminating the joint venture. The arbitration hearings were held in Stockholm—on neutral ground. These were the first major arbitrations involving a multinational corporation and a Chinese state-owned company since China's entrance into the WTO in 2001. One of the arbitrators selected by PepsiCo, Dr. Wang Shengchang, was a Chinese national. He voted in favor of PepsiCo and, coincidentally, in March 2006 was apprehended and has been detained ever since.[5]

FIREMAN'S FUND

One of my deepest frustrations over so many international trade agreements has been the unwillingness of our trading partners to fulfill their obligations.

For example, Fireman's Fund, which is a very large insurance company in my State of California, purchased $50 million in debt securities from a Mexican Bank in 1995. At the same time a similar debt purchase was made by Mexican Investors. When the bank began to experience financial difficulties in about 1997 the Mexican Banking and Financial Authorities allowed the Mexican investors to redeem their notes, while denying the same treatment to Fireman's Fund. In my view, this is a case of blatant discrimination which should not be allowed to occur.

Because it is a matter involving a financial institution, Fireman's Fund is not allowed to bring a NAFTA Action on its own and must instead rely upon the U.S. government to pursue this. All efforts by the U.S. government to convince the Mexican government of the inequities of their position have gone unanswered. The factual record of this strongly supports Fireman's Fund.

Indeed, a NAFTA tribunal which ruled on an underlying expropriation case in 2006, said that the facts clearly reveal that Fireman's Fund was the victim of a severe injustice.

WHAT IS THE U.S. RESPONSE?

The scope of U.S. assistance in these cases consists of helping the U.S.-owned company navigate the host country's legal system. The irony is clear.

Under limited circumstances, and coordination with the Justice Department, the State Department *may* authorize a consular officer to appear before a foreign court or tribunal to request a suspension of proceedings to give the U.S. citizen time to obtain legal representation, but nothing more.[6]

Simply put, the government too often does not take any specific course of action to directly assist US companies and investors, even in situations where it is known that the legal system does not work.

Commerce's Office of Market Access and Compliance does offer U.S. businesses a Trade Complaint Hotline through its TCC On-line application for assistance on commercial disputes in host countries. However last year, the Office of Market Access and Compliance was able to resolve only 54% of its cases.[7]

---

[4] Ashby Jones & Andrew Batson, The Wall Street Journal; Concerns about China arbitration rise; found on http://www.newspress.com/Top/Article/article.jsp?Section=BUSINESS&ID=565294941409181704 (May 9, 2008)

[5] Ashby Jones & Andrew Batson, The Wall Street Journal; Concerns about China arbitration rise; found on http://www.newspress.com/Top/Article/article.jsp?Section=BUSINESS&ID=565294941409181704 (May 9, 2008)

[6] CRS Report : U.S. Government Assistance on Foreign Investment Disputes, M. Angeles Villareal, July 9, 2008; Page # 2

[7] CRS Report : U.S. Government Assistance on Foreign Investment Disputes, M. Angeles Villareal, July 9, 2008; Page # 5

LACK OF RESOURCES

Clearly a lack of staffing may be part of the problem. The Departments of State and Commerce are being asked to handle ever increasing demands on their resources. The number of Free Trade Agreements grew dramatically in the last 10 years, for example, and our overall trade and trade deficit have exploded, while staff levels have either decreased or stagnated.[8] [9]

I am eager to hear from our witnesses today on what changes the U.S. Government can adopt within its various trade agencies to ensure that all American businesses and investors, whether their dispute is with a foreign company or a foreign government, whether it is with an FTA country or a country like China, have the resources to guarantee they will have fair treatment overseas.

Mr. ROYCE. Well, I thank you very much, Chairman Sherman for holding this hearing at my request. Your consideration on this is very much appreciated by me.

Today, we are supposed to be looking at the tools that our Government can bring to bear when U.S. businesses run into trouble overseas. I think all Members of Congress have been contacted by businesses in their district that have been victimized abroad at one point or another. We hear about how contracts are broken, and no local enforcement occurs.

So this happens in many parts of the world. But I will tell you, for me and for my colleagues from Southern California, what concerns us is the fact that the vast majority of them have to do with fleecing our constituents and the amount of fraud committed on our constituents in Southern California who make investments in China, who make investments in Shanghai and Beijing.

It is a safe bet that the number of these problem cases are going to grow as global trade and investment expands, and U.S. companies sell more abroad. This hearing is a chance to gauge how well the State and Commerce Departments and other U.S. Government agencies with commercial portfolios perform when going to bat for American firms.

The onus is always on the investor. Caution, we know, is always in order. But Americans investing abroad should know if their government is wielding a slugger or a toothpick in these situations.

I think there is a certain responsibility on the part of the media to report an investment climate. So when the hype is going on, the investor knows what type of reception they are going to get when they get over there and make that investment in that country.

When a reporter says that, you know, we cannot cover every one of these cases, because it would take up the entire newspaper every day to report on the amount of fraud going on in China, then I think it is time we take a look at it.

Now I am glad that we are hearing from a businesswoman who has been on the front lines today. I have recently become aware of this case of Nancy Weinstein, who is from Southern California, who has attempted to do business in Shanghai, China, where she has encountered harassment and abuse.

Her case, I think, is a big red flag for those seeking to take advantage of the opportunities that on paper exist in China. Because

[8] The estimated staff dedicated to goals that include monitoring and enforcement of these trade agreements currently sits as such: Commerce with 602 and State with 775.

[9] GAO, International Trade: Further Improvements Needed to Handle Growing Workload for Monitoring and Enforcing Trade Agreements, GAO-05-537, (Washington, D.C.: June, 2005)

unfortunately, the reality is often very different than what appears on paper.

Nancy has seen her contract broken, her property stolen, and has even suffered physical intimidation. Chinese Government authorities appear complicit. This business person, after much blood, sweat, and tears, is now out millions and millions of dollars; and she is not alone. Because of this hearing, I have heard from many others with similar bad stories from China. I have got to tell you, over the last few years, I have heard some incredible stories about what happened to Southern Californians who have attempted to invest there.

Now today, I would like to focus on what the State Department and other U.S. Government agencies have done on behalf of Nancy for sure; but also the many other American businesses that have had nightmares in China. As Ms. Weinstein will testify, "There are too many greedy, well connected Chinese business guys in China that pay off the right people and get what they want, and we have no recourse."

Would-be American investors should understand the environment that they are jumping into. If our Government is going to provide commercial service, it ought to give accurate and prominent warnings about China and elsewhere; and fight darn hard when there is a problem like the one we will hear about today. I am concerned that tools such as visa denials are not being used.

Our Government should guard against hype when it comes to foreign investment, particularly in China. Too many investments have gone wrong—not defeated by market competition, but instead defeated by cronyism, defeated by corruption.

The administration right now is negotiating a bilateral investment treaty with China. I hope it would contain meaningful investor protections in it.

But regardless, I am concerned that the message given by this treaty, and reinforced by our Government's commercial apparatus, is encouraging of the Chinese market at the expense of a realistic appraisal of the difficult conditions foreign businesses face when we go overseas. I really think the business press has a responsibility to carry some of these stories.

You know, sometimes the challenges our Government speaks about are better seen not as challenges; but rather as mine fields. Again, I thank you, Mr. Chairman, and I look forward to hearing from our witnesses today.

Mr. SHERMAN. Are there others who wish to make an opening statement?

[No response.]

Mr. SHERMAN. Seeing none, we will move on to our witnesses. Our first panel includes David Nelson. He is the Principal Deputy Assistant Secretary for International Finance and Development within the Bureau of Economic, Energy and Business Affairs at the U.S. Department of State.

He manages the International Finance and Development Branch, overseeing the advancement of sustainable economic growth and development broad by enhancing investment climates.

I also want to welcome, I believe, again, Israel Hernandez, the Assistant Secretary for Trade Promotion and Director General of

the U.S. and Foreign Commercial Service. He is the U.S. Government's point of contact for trade promotion and business advocacy assistance. Prior to his confirmation, Mr. Hernandez served as Senior Advisor to the Secretary of Commerce.

Let us hear first from Mr. Nelson, and then from Mr. Hernandez.

STATEMENT OF MR. DAVID D. NELSON, PRINCIPAL DEPUTY ASSISTANT SECRETARY, BUREAU OF ECONOMIC, ENERGY AND BUSINESS AFFAIRS, U.S. DEPARTMENT OF STATE

Mr. NELSON. Thank you, Mr. Chairman.

Chairman Sherman, Ranking Member Royce, members of the committee, thank you for giving me this opportunity to discuss how the State Department helps Americans resolve foreign, commercial, and investment disputes. I have submitted written testimony. Please allow me to briefly summarize my key points.

First of all, we believe that investment abroad promotes U.S. and global economic growth. It creates jobs both here and in the recipient country, enhances prosperity, and fosters political stability in recipient countries.

U.S. businesses invested over $216 billion worldwide in 2006. This is good for our economy; in part, because U.S. foreign direct investment serves as a magnet for U.S. exports and, therefore, increases U.S. job growth. About one-fifth of U.S. exports and intrafirms ships to affiliates abroad.

The State Department is committed to support U.S. investors and business overseas as a core diplomatic in-concert function and a top priority of all our Embassies. The State Department works in close coordination, both here and overseas, with our colleague at the Commerce Department. So I am pleased we are here together to discuss jointly how we assist U.S. business and individuals involved in disputes abroad.

Our policy to address commercial investment disputes has three primary elements. First, State Department representatives and colleagues from other agencies at Embassies around the world seek to provide as much information and assistance as possible to U.S. citizens exploring investment and business opportunities.

To this end, the department furnishes a broad range of services, including researching and publishing annual, country-specific investment climate statements; providing briefings to U.S. business; and suggesting and facilitating appropriate local contacts in business and government.

Our job is to convince particular firms to invest abroad; but rather to give Americans our best insights into the local situation, including risks as well as opportunities, so they make their own informed choices.

Mr. Chairman, you mentioned the desire of publishing information about problems abroad. In my written comments, I include a description of the investment climate statements, which we publish on an annual basis. We do not sugarcoat these reports.

For example, the February 2008 Russian investment climate states, "According to numerous reports, corruption in the judicial system is widespread and takes many forms, including bribes to judgments and prosecutors, and fabrication of evidence."

The February 2008 China investment climate statement is available on the Web and available through the Commerce Department, as well as the State Department. This statement provides, "Investors continue to face an unreliable legal system, incapable of guaranteeing the sanctity of contracts."

So our first step is to provide the best information we can, as realistic as we can make it. Secondly, we provide a variety of services to U.S. nationals in the event they do become involved in commercial disputes with private parties or investment disputes with foreign governments.

Our mission is to distribute information about local attorneys who have indicated an interest or experience in representing officials. We also describe remedies that may be available under bilateral investment treaties or other international agreements or through domestic legal procedures.

We help provide information about how to contact relevant host government officials, and offices that can be of assistance to U.S. citizens in their efforts to resolve claims.

Where appropriate, the State Department engages in active diplomacy with foreign officials to emphasize the importance of resolving commercial investment disputes fairly, in accordance with due process of law. Oftentimes, a simple inquiry by U.S. Government officials for more information on the statute of a case yields positive results for the U.S. investor.

Third and more broadly, we promote more open and transparent investment environments to enhance protections and increase market access for U.S. investors abroad. This includes a variety of steps, including negotiating bilateral investment treaties, and investment chapters and free trade agreements that create important substantive protections, and allow U.S. investors to bring investment claims directly against the host state in binding international arbitration.

This is particularly important, considering that more and more Americans are pursuing investment opportunities in emerging markets abroad that provide attractive returns, but increased risks.

For example, we did recently launch negotiations with China. We believe that a good agreement with China will enhance the protections available to American investors in that country.

Mr. Chairman and members of the committee, I have given you today an overview of the policies of the administration and strong commitment of the Department of State to help U.S. citizens resolve investment disputes abroad. Thank you for giving me the opportunity. I will be happy to answer your questions.

[The prepared statement of Mr. Nelson follows:]

PREPARED STATEMENT OF MR. DAVID D. NELSON, PRINCIPAL DEPUTY ASSISTANT SECRETARY, BUREAU OF ECONOMIC, ENERGY AND BUSINESS AFFAIRS, U.S. DEPARTMENT OF STATE

Chairman Sherman, Ranking Member Royce, Members of the Committee, thank you for giving me this opportunity to discuss how the State Department helps U.S. nationals resolve foreign commercial and investment disputes.

U.S. portfolio and foreign direct investment abroad promotes U.S. and global economic growth, creates jobs both here and in the recipient country, enhances prosperity and fosters political stability in recipient countries. In 2006, the stock of U.S. foreign direct investment abroad exceeded $1.8 trillion, and U.S. businesses invested over $216 billion worldwide in that year. U.S. foreign direct investment serves as

a magnet for U.S. exports and increases U.S. job growth. In 2005, U.S. multinationals exported $491 billion, accounting for more than 54 percent of total U.S. exports. Nearly half of this amount, $189 billion, was exported to their foreign affiliates. In the same period, U.S. companies with foreign affiliates enjoyed a faster rate of domestic U.S. employment growth than U.S. companies as a whole.

The instructions every Ambassador receives before assuming his or her responsibilities emphasize that support for U.S. investors and businesses overseas is a core diplomatic and consular function and a top priority for all U.S. economic agencies. To assist this mission, the Department of State is committed to supply the best information available to U.S. businesses contemplating doing business, including investing, overseas and to provide vigorous advocacy and support for U.S. businesses operating in the overseas environment. State also works in close coordination both here and overseas with our colleagues at Commerce, so we are pleased that they join us today to provide additional insights into how U.S. businesses and individuals involved in disputes can be assisted.

In addition to direct assistance for U.S. persons, the Department encourages foreign governments to undertake reforms to improve their business and investment climates and to provide fair, nondiscriminatory and transparent operating conditions for U.S. businesses. Where necessary, the United States encourages foreign governments to become "responsible stakeholders" that will work with the United States to sustain and advance an open and fair global investment and trade environment.

U.S. POLICY ADDRESSING COMMERCIAL AND INVESTMENT DISPUTES

U.S. policy to address commercial and investment disputes involving U.S. nationals has three primary elements: First, the Department provides pre-investment guidance including commercial guides and investment climate information, in-country commercial and business environment briefings and business outreach assistance to U.S. businesses, investors, and property owners abroad. Second, the Department provides information and assistance to U.S. investors and property owners that may be engaged in a dispute. Assistance includes providing local attorney lists maintained by the Consular section and exploring remedies that may be available under bilateral investment treaties (BITs) or other agreements, or through local domestic procedures. Where appropriate, the State Department engages in active diplomacy with foreign officials to emphasize the importance of resolving commercial and investment disputes fairly, in accordance with due process of law. Third and more broadly, the State Department promotes more open and transparent investment environments through encouraging States to become parties to key international conventions related to the resolution and enforcement of investment disputes, as well as setting investment policy standards and guidelines through important multilateral organizations. The Department also negotiates with other governments to conclude bilateral investment treaties ("BITs") and investment chapters in free trade agreements which provide enhanced protections for U.S. businesses when they engage in foreign direct investment and other forms of investment abroad.

ASSISTANCE TO U.S. BUSINESSES, INVESTORS, AND PROPERTY OWNERS

First I will talk about the State Department's work to provide pre-investment support, information and advocacy for U.S. businesses, investors and property owners entering foreign markets. Then I will discuss how Department serves U.S. investors, businesses, and property owners involved in disputes with private individuals or with government entities and distinguish the particular support and options the Department is able to provide to investors with claims against a foreign government.

State Department representatives at Embassies around the world seek to provide as much information and assistance as possible to U.S. Citizens involved in investment, trade agreement compliance and other business-related activities.

To this end, the Department furnishes a broad range of services, including: researching and publishing annual, country-specific investment climate statements, providing business pre-briefings for U.S. nationals, suggesting and facilitating appropriate local business and government contacts for new businesses or investments, and indicating consular and other assistance available to U.S. businesses and individuals in case they become involved in a commercial or investment disputes abroad. These services provide information relevant to the initial investment decision, but also to business decisions such as legal or regulatory options that may be pursued in the event a dispute arises. Specifically, the Department monitors and shares relevant information about foreign laws, judicial systems, property ownership, regulatory transparency, corruption and claims procedures. The Department

also shares relevant information on how U.S. claimants can pursue relief for commercial and investment disputes through local domestic procedures as well as what recourse may be available under an applicable bilateral investment treaty or otherwise through arbitration.

The Embassy or Consulate may also share information on prior disputes, known criminal activity and other important investor information. Investor pre-briefs can be a valuable tool should the investor choose to avail him or herself of the tool. For example, in seven cases in the last year, the Commercial Service (CS) in Beijing helped clients to identify that their potential Chinese partners were actually parts of scams. CS Beijing was able to protect U.S. companies from signing contracts with fraudulent Chinese companies.

Investment Climate Statements are another useful tool which strives to give the full picture of a country's investment climate—including the challenges of doing business. We do not sugarcoat these reports. For example, the February 2008 Russia Investment Climate Statement states, "According to numerous reports, corruption in the judicial system is widespread and takes many forms, including bribes to judges and prosecutors and fabrication of evidence." The February 2008 China Investment Climate statement provides: "Investors continue to face an unreliable legal system incapable of guaranteeing the sanctity of contracts." State Department Investment Climate Statements are part of the individual Country Commercial guides published by Commerce on their website, www.buyusa.gov.

The Department provides a variety of tools and services to U.S. nationals in the event they become involved in commercial business disputes with private parties or investment disputes with a foreign government. The Department distributes information about local attorneys who have indicated an interest or experience in representing U.S. nationals abroad to U.S. claimants and views this as an essential Consular function. The Department also provides information about how to contact relevant host government officials and offices that can be of assistance to U.S. Citizens in their efforts to resolve their claims. Embassy or Consular officials may also facilitate such contacts and urge the foreign government to ensure that the dispute is resolved expeditiously and in accordance with local law.

Oftentimes, an inquiry by USG officials for more information on the status of the case yields positive results for the U.S. claimant. For example, a U.S. airplane leasing company in Indonesia was unable to retrieve its leased planes from an Indonesian airline in default. The Ministry of Transportation delayed de-registering the planes well past its official 60-day regulatory deadline. Without de-registration, the U.S. lessor could not remove the planes from Indonesia. The U.S. company also detailed rumors of commercial relationships between the defunct airline and ministry officials. The Embassy Transportation officer spoke to three government official contacts at the Ministry on a variety of occasions seeking information and status on the case, and reminded host officials that even the appearance of unfair treatment by host officials could negatively affect the investment environment, especially an environment in which there was an international plane shortage and a rapidly growing domestic airline industry. The planes were returned and deregistered in six months.

Our colleagues in the Department of Commerce are heavily involved in business briefing and commercial disputes through the Commercial Service (CS) offices located in over 80 larger U.S. consulates and Embassies overseas. They will be able to describe the additional support the CS can provide. State and Commerce Foreign Service Officers work closely together on economic and commercial issues at Embassies and Consulates. In Posts with CS offices, a commercial officer may take the lead in monitoring and interacting with a U.S. national who would like to invest or who is already involved in a commercial dispute. State colleagues may provide attorney lists maintained by the Consular section, relevant foreign government or other contacts, and facilitation of such contacts. In the past, and subject to staff availability, Commerce and State Department officers have sat in as observers at court proceedings.

The U.S. is the world's largest investor. More and more Americans are pursuing investment opportunities in emerging markets that provide attractive returns, but increased risks. From 2003 to 2006, U.S. foreign direct investment abroad grew from $129 billion to $216 billion. In China alone, U.S. investment doubled from $11 billion in 2002 to $22 billion in 2006. Embassies and Consulates also report an increase in commercial and investment disputes, but note that the number of cases is relatively low compared to the number of investors. For example, CS Shanghai noted 22 disputes in the past year, while the American Chamber of Commerce in Shanghai noted its membership rolls have increased to 3,500 U.S. affiliated companies in the same time period. Although U.S. investors face a difficult investment environment in China, of 618 U.S. companies surveyed by the American Chamber of

Commerce in 2007, 89 percent expressed their five-year outlook about business in China as "optimistic" or "cautiously optimistic."

ASSISTANCE WITH INVESTMENT DISPUTES INVOLVING ANOTHER GOVERNMENT

The Department may also actively provide diplomatic assistance to U.S. nationals involved in investment disputes—that is, disputes against a host country relating to a U.S. business's investment in the host country's territory. The Department encourages active Embassy reporting on, and involvement in claims and disputes of, U.S. nationals against foreign governments. It has strengthened coordination in Washington of assistance to U.S. nationals, on occasion has sent experts to meet with other governments and assess claims resolution progress, and has encouraged other governments to adopt procedural avenues for investors to seek redress. The resolution of investment disputes is a priority for the Department.

As with commercial disputes involving private parties, U.S. claimants bear the primary responsibility for pursuing resolution of their investment disputes through the local court system or through arbitration, where available. While the U.S. investor is pursing a remedy in local courts, the U.S. Government may and, where appropriate, does engage diplomatically with the host government in order to encourage expeditious and fair resolution of the dispute. The level and degree of such assistance may take a variety of forms. In some cases, a diplomatic intervention may require only an informal inquiry, such as alerting relevant ministries to the existence of a particular dispute. In other cases, U.S. officials might urge a host government to identify an appropriate official with authority to address and resolve a dispute, or encourage an official to meet with an investor. The United States might also encourage both parties to consider some third-party dispute resolution mechanism, if available, such as the International Centre for the Settlement of Investment Disputes (ICSID), the Multilateral Investment Guarantee Agency (MIGA), or a private arbitration service such as may be provided by a regional chamber of commerce or similar organization. In other cases, it may be appropriate to remind the host government of its obligations under international law generally and specifically under treaties to which it is a party. Diplomatic interventions in support of investors in such instances can be and are pursued at the highest levels of the U.S. Government.

Where the United States has concluded a bilateral investment treaty (BIT) or a free trade agreement (FTA) investment chapter with the host government, and where the dispute falls within the scope of the agreement, U.S. claimants may wish to pursue their claims directly against the host State through international arbitration. The United States has 40 BITs in force and comparable provisions apply with the 12 countries that are Parties to U.S. free trade agreements with investment chapters. The Administration is actively seeking to expand the number of countries with which we have such agreements, as evidenced by our conclusion of a BIT with Rwanda in February, and our launch of BIT negotiations with China and Vietnam in June. Where an investment dispute arises in a country that is a party to a U.S. investment agreement, U.S. officials are happy to provide an aggrieved U.S. investor a copy of the agreement and will encourage the investor to seek legal counsel to determine whether the agreement might be useful in resolving the dispute.

In countries where no BIT or FTA investment chapter is in force, other remedies may be available to the U.S. investor under customary international law. Under certain circumstances, the U.S. Government may be entitled to espouse the investor's claim, that is, formally present the claim, on the investor's behalf, to the foreign government for resolution as a diplomatic matter. Before considering whether to do so, however, the U.S. investor must meet certain criteria, including that it was a U.S. national from the time the claim arose through the resolution of the claim, that the claim is based on a violation of international law attributable to the host State, and the investor has pursued all available local remedies unsuccessfully, or demonstrated that doing so would be futile.

The requirement that a claimant exhaust all available local remedies, in particular, is required under international law and supported as a matter of policy by the United States. Exhaustion means that the investor must pursue all avenues of redress which are reasonably available, presenting all available evidence to local courts, and appealing adverse decisions of lower courts when possible. This step allows the host government an opportunity to provide redress through its own legal system, helps refine issues of fact and law, and avoids unnecessary international disputes between governments. In addition, as a matter of international comity, this step helps to avoid one government second guessing another government's ability to provide a judicial or administrative resolution of a dispute or otherwise sitting in judgment of the official acts of that government.

Under international law, if an investor can demonstrate that pursuit of a remedy through a national court system would be ineffective or futile, he may be excused from the requirement to exhaust local remedies. A determination of ineffectiveness or futility can only be made on a case-by-case basis, but would at least require, for example, convincing evidence of systematic corruption. The Department carefully evaluates the claims of U.S. investors brought before it to determine whether there is evidence of futility before taking a position on the merits of the dispute.

With regard to claims by U.S. citizens for expropriations by foreign governments, the Department prepares and submits an annual report to Congress (pursuant to section 527(f) of the Foreign Relations Authorization Act (the "FRAA")) detailing expropriation and other noteworthy investment disputes of U.S. citizens against foreign governments. In certain cases and in coordination with other U.S. agencies, the Department's strategy calls for the possible withholding of benefits in response to expropriations or other foreign government actions that meet the law's criteria. In 2007, the number of countries against which U.S. nationals face these type of investment claims presented to the Department has risen to 88, a 24% increase from 2004. The Department followed a total of 363 cases in 2007 (an 8% increase for the same period). Close cooperation with governments, regular meetings between senior U.S. Government and foreign government officials, and constant work with U.S. citizen claimants has resulted in the steady and significant resolution of many of these pending property claims.

In certain investment dispute cases, under Section 2225 of the Foreign Affairs Reform and Restructuring Act of 1998, the Secretary of State has the authority to deny visas to an alien who, through the abuse of official position, converts for personal gain confiscated or expropriated real property to which a U.S. national owns a claim. Section 2225 is a valuable tool discouraging the conversion of expropriated or confiscated real property for personal gain, and in appropriate cases, can help to facilitate the resolution of outstanding claims, particularly in countries with unresolved cases of expropriation of the real property of U.S. Citizens. In practice this Section 2225 has been applied against Nicaragua. There are currently nine Nicaraguan visa denial cases as of April 2008. In most cases expropriation claims are either resolved through diplomatic efforts or through local or international arbitration, and a step like the 2225 visa ineligibility determination is not needed.

U.S. DEVELOPMENT OF OPEN AND FAIR INVESTMENT ENVIRONMENTS

More broadly, the Department has played a key role in negotiating multilateral agreements that can assist investors in enforcing the arbitral awards that resolve their investment disputes. These include the Convention on the Settlement of Investment Disputes between States and Nationals of Other Countries (the Washington Convention), which came into force on October 14, 1966, and which established the International Centre for Settlement of Investment Disputes (ICSID). Pursuant to the Convention, ICSID provides conciliation and arbitration facilities for the settlement of disputes between member countries and investors who qualify as nationals of other member countries. Under U.S. BITs, U.S. investors have the option of choosing to resolve their disputes before an ICSID arbitral tribunal.

Another example of a multilateral agreement that may assist U.S. investors is the Convention on the Recognition and Enforcement of Foreign Arbitral Awards concluded in New York. The New York Convention, as it is commonly known, obligates the local courts of State Parties to recognize and enforce arbitral awards rendered outside their jurisdiction in accordance with fair and uniform standards. Together, these conventions offer U.S. investors an additional line of protections, remedies, and enforcement mechanisms. Persuading states to accede to these conventions is a long-standing element of U.S. foreign policy. To date, there are 143 parties to the Washington Convention and 142 parties to the New York Convention.

The Department also encourages open investment regimes through its leadership of U.S. engagement with the Investment committee of the Organization for Economic Cooperation and Development (OECD). The Department participates in the OECD to develop rules and practices for international investment agreements, investment regime liberalization, and prevention of investment protectionism. The OECD also engages with non-member countries, such as India, China, Brazil, and Indonesia, through "enhanced engagement" partnerships in order to garner participation and support for broad-based open investment practices and policies in these countries.

The Department promotes open and transparent economies and increased opportunities for U.S. businesses and individual investors through high-level dialog with foreign governments. The June 2008 Strategic Economic Dialogue between cabinet-level U.S. and Chinese government officials yielded commitments for negotiations of

a Bilateral Investment Treaty and inauguration of an "Investment Forum" to review investment screening mechanisms that are often barriers for U.S. investment.

Finally, but perhaps most importantly, the Department encourages the development of nondiscriminatory, open, and market-oriented investment environments for U.S. investment overseas through active negotiation of bilateral investment treaties (BITs) and free trade agreement investment chapters. BITs and FTA investment chapters protect U.S. investors and investments abroad and help promote greater access for U.S. investors in foreign markets. These treaties and agreements create important substantive protections and allow U.S. investors to bring investment claims directly against the host State in binding international arbitration. The protections afforded U.S. investors are comparable to those foreign investors enjoy under U.S. law, and the right to binding arbitration may provide important leverage to U.S. investors in resolving their disputes with foreign governments.

Mr. Chairman and members of the Committee, I've given you today an overview of the policies of this Administration and the strong commitment of the Department of State towards helping U.S. Citizens resolve investment disputes abroad.

Thank you for giving me the opportunity to come and share our thoughts with you. I will be happy to answer your questions.

Mr. SHERMAN. Thank you; Mr. Hernandez?

STATEMENT OF THE HONORABLE ISRAEL HERNANDEZ, ASSISTANT SECRETARY FOR TRADE PROMOTION AND DIRECTOR GENERAL OF THE U.S. AND FOREIGN COMMERCIAL SERVICE, INTERNATIONAL TRADE ADMINISTRATION, U.S. DEPARTMENT OF COMMERCE

Mr. HERNANDEZ. Chairman Sherman, Ranking Member Royce, and distinguished members of the committee, thank you for the opportunity once again to speak to you about how the Department of Commerce assists U.S. companies with commercial disputes in foreign countries.

The mission of the Commerce Department, International Trade Administration, is to help assure the continued ability for U.S. firms to compete and win in the global market place; and to create prosperity by strengthening the competitiveness of U.S. industry promoting trade and investment, and ensuring fair trade and compliance with trade laws and agreements.

I have the privilege of leading a field-based network of trade professionals, located in 107 cities in the United States and 76 countries who provide commercial diplomacy and trade promotion support to U.S. companies.

We are often the first part of the U.S. Government that companies come to when they have a trade or investment-related problem. We estimate that over half of our officers' time is spent working to facilitate resolution of these issues.

Companies encounter problems with governments and their private sector counterparts in every country around the world, as you mentioned, including here in the United States. The nature of the disputes vary by location, as U.S. companies must operate in the local environment that they are in.

In Mexico, our commercial offices reported the most common type of assistance they give U.S. companies involves payment disputes with local Mexican companies.

In Brazil and in India, our offices report that the most frequent problem U.S. companies deal with is a complex maze of bureaucratic regulations.

In China, the problems U.S. companies face vary from a lack of transparent regulations, to weak IPR enforcement, to uncertain judicial processes.

When a company comes to one of our overseas posts, a domestic field office, or an ITA trade specialist in Washington, complaining that it has been unfairly treated by a foreign government, we will often address this issue through government-to-government diplomacy.

When a company's problem involves an issue covered by a trade agreement, ITA's trade agreement's compliance program brings together all relevant U.S. Government experts to analyze the issue, verify the information, and develop an action plan for addressing the concern.

ITA's staff are currently working on 200 active cases, to assist U.S. companies to gain market access in countries that are parties to a trade agreement with the United States.

Our approach is different with a U.S. company that involves a commercial dispute with a local private sector company. We encourage our team to meet with the U.S. company and the foreign company to provide assistance appropriate to the circumstances.

Once a case enters the foreign court system, we are limited in our ability to help the U.S. company. We provide a local list of attorneys recommended by the Embassy. We share information about the judicial system, or possible dispute resolution procedures, and provide information about how to contact host government officials.

Our overseas staff can mention the dispute to government officials and business associations, which can have an impact, as local officials do not want their region to be seen as hostile to business investment.

However, the most important thing we can do to help U.S. companies is to try to prevent that likelihood of their involvement in a business dispute. This involves educating and counseling U.S. companies about local business issues, and working with foreign governments to affect changes to make their commercial environments more hospitable for all companies.

We urge U.S. companies to study the export market, and familiarize themselves with a business climate, in order to have a strong understanding of both the opportunities and the challenges. This type of due diligence is essential.

There are a number of ways we work to ensure U.S. companies are aware of potential business issues in foreign markets. While I have a more extensive list in my written testimony, let me highlight it for you.

First, trade specialists in our domestic office frequently counsel individual companies, as well as conduct local outreach seminars to the U.S. business community, both about the opportunities and challenges of entering foreign markets.

Second, when a U.S. company arrives in a country to do business, and they have not contacted our domestic office, the economic or commercial team at post often provides a briefing on the unique issues the company will face in market.

Third, U.S. companies can easily access a number of resources by calling the Trade Information Center, Trade Help Line, 1–800–

USA–TRADE, to speak to regional experts or log on to the Web site, www.export.gov, to learn more about each market of interest.

Finally, our Trade Compliance Center regularly provides training to U.S. officials in the field and conducts outreach activities to raise awareness of ITA's Trade Agreements Compliance Program among U.S. firms, and identifies firms that have encountered problems.

In addition, to directly assist U.S. companies, the Department of Commerce coordinates closely with U.S. Government agencies to work with foreign governments to improve their business environment.

For example, the U.S./China Joint Commission of Commerce and Trade, the JCCT, has made progress in helping resolve software piracy issues. The Chinese now have agreed to pre-load legal operating systems software on all computers produced or imported into China.

We also have commercial dialogues, government-to-government, on issues by each country with a private sector in Russia, in Brazil, and in India.

Senior Commerce Department officials often travel to these countries so that we can support U.S. companies as they experience problems consistent with a lack of a rule of law. In such countries, we often raise the need to develop a predictable and transparent legal system through our foreign counterparts.

In conclusion, Mr. Chairman, we have a robust system for helping U.S. companies when they have problems overseas. We are focused on assisting them with current issues, and working with foreign governments to prevent problems from occurring in the first place.

We have positioned both our overseas staff and our policy focus toward addressing the most common problems U.S. companies face in markets where we are needed most. Our goal is to enhance the U.S. companies' international experience and success, so that exporting becomes an intrical part of its business.

Thank you for your time, and I am more than happy to answer any questions you may have.

[The prepared statement of Mr. Hernandez follows:]

The Honorable Israel Hernandez
Assistant Secretary for Trade Promotion and Director General of the United States and Foreign Commercial Service
International Trade Administration, U.S. Department of Commerce
Testimony Before the United States House Committee on Foreign Affairs
Subcommittee on Terrorism, Nonproliferation, and Trade
"Aiding American Business Abroad: Government Action to Help Beleaguered American Firms"
July 17, 2008

Chairman Sherman, Ranking Member Royce, and distinguished members of the Committee, thank you for the opportunity to speak to you today about how the United States Department of Commerce assists U.S. companies with commercial disputes in foreign countries. I welcome the Committee's focus on this topic, and its continued dedication to supporting policies and programs intended to strengthen our nation's exporters.

The mission of the Department of Commerce's International Trade Administration (ITA) is to help assure the continued ability of U.S. firms and workers to compete and win in the global marketplace and to create prosperity by strengthening the competitiveness of U.S. industry, promoting trade and investment, and ensuring fair trade and compliance with trade laws and agreements.

ITA plays a key role in supporting and advancing the Administration's trade agenda – seeking to expand commercial opportunities for American firms through free and fair trade at the bilateral, regional, and multilateral levels. ITA works to promote U.S. exports, remove trade barriers, ensure foreign compliance with trade agreements, enforce trade laws, and enhance the competitiveness of U.S. industry at home and abroad. Our trade team is stationed in over 230 offices domestically and internationally and is organized into four program areas: Manufacturing and Services (MAS), Market Access and Compliance (MAC), Trade Promotion and the U.S. & Foreign Commercial Service (CS), and Import Administration (IA). Today, I would like to focus on the activities of the first three, each of whom is dedicated to the global competitiveness of U.S. industry through promoting exports, opening markets abroad, and ensuring that our trade agreements throughout the world are respected and enforced.

As ITA's Assistant Secretary for Trade Promotion and Director General of the U.S. and Foreign Commercial Service, I have the privilege of leading an organization dedicated to helping U.S. companies, especially small and medium-sized enterprises (SMEs), compete and win in the global economy. We are a field-based network of trade professionals located in 107 U.S. cities and over 126 overseas offices in 76 countries who provide commercial diplomacy and trade promotion support to U.S. companies. We guide companies through every step of the export process, from shipping and logistics to learning about foreign regulations. We offer trade counseling and advocacy and customized solutions to enter new markets and overcome exporting

hurdles. Because of our field presence, we are often the first part of the U.S. Government that companies come to when they have a problem. We estimate that over half of our officers' time is spent working to facilitate resolution of U.S. company problems.

Businesses come to us with a variety of issues, but many are either problems involving a foreign government or commercial disputes. Bureaucratic obstacles can involve goods stuck in port over documentation problems, not having a certificate from the relevant Ministry, or being removed from the foreign government-approved short-list on an infrastructure project. Commercial disputes with local companies frequently involve payment issues or an alleged intellectual property rights violation.

Government Disputes

When a company has a problem involving a foreign government, we employ a variety of means to address the issue through direct government–to–government channels and commitments made through trade agreements.

If a company comes to one of our overseas posts, a domestic field office, or an ITA trade specialist in Washington, complaining that it has been unfairly treated by a foreign government, and we determine that the issue is not covered by a trade agreement, we will often address this issue through government-to-government diplomacy.

For example, last August, an Ohio-based electronics manufacturer, requested Commercial Service Warsaw's help with obtaining a permit from the Ministry of Interior. The company had sought to acquire a Polish manufacturer of electrical power components and needed permission to purchase the land on which the factory was built. The Ministry had held the company's application without action for three months and further delays threatened to jeopardize the $7 million deal. In an effort to prevent further delay, our team contacted working-level Ministry officials, urged them to process the application promptly, and tracked the matter through the bureaucratic channels. CS Warsaw also engaged the Embassy's Legal Attaché to make simultaneous appeals with Ministerial contacts. Within a month, the Polish Ministry of Interior approved the company's purchase of land, and the parties successfully concluded the transaction.

When a company's problem involves an issue covered by a trade agreement, ITA's Trade Agreements Compliance Program, led by our Market Access and Compliance unit, works with the client to develop a strategy for addressing the complaint. We bring together all relevant Department of Commerce, and if necessary, U.S. Government, experts so the company does not have to go to several different government agencies for assistance in finding a solution to their concern. This team of experts analyzes the issue, verifies the information, and develops an action plan for addressing the concern. This team has the ability to elevate the issue to bring the full weight of the U.S. government to bear on the U.S. company's behalf.

ITA staff are working on approximately 200 active cases to assist U.S. companies gain market access in countries that are parties to a trade agreement with the United States (the term "trade agreements" includes both bilateral and multilateral agreements). From FY 2001 through 2007, we initiated over 630 compliance cases and closed over 460 of them where agreements were involved, including nearly 160 that were resolved successfully.

For example, a small Florida company that refurbishes copier equipment and parts reported on the Trade Compliance Center (TCC) Hotline that a shipment of its goods were being held in Chilean Customs. The company believed that the shipment was being held due to a competitor lobbying Chilean Customs, and asked for USG assistance. The TCC alerted relevant DOC experts, including the Department's Chile desk officer, who called the company directly to obtain additional information. The desk officer determined that the company had improperly filled out the certificate-of-origin for claiming preferential treatment under the U.S.-Chile FTA and provided the company with resources, including a specialist at the U.S. Embassy in Santiago, to assist in filling out the paperwork and getting the shipment released. A Commercial Service officer in Chile then contacted the company's agent and Chilean Customs, who said that the company would have to pay a steep fine to obtain release of the goods. The Embassy consulted with the team in Washington, including an expert on rules-of-origin issues, and determined that Article 4.16.4 of the FTA states: "A Party shall not subject an importer to penalties where the importer that made an incorrect declaration voluntarily makes a corrected declaration." Chilean Customs reversed its earlier decision to fine the company for incorrectly claiming preference under the FTA and released the shipment. The company stated that the team's assistance in speaking with Chilean Customs was "absolutely key" in getting the container released.

In another case last year, Kazakhstani Customs interpreted an amendment to the Kazakhstani Customs Code to require importers of U.S. goods to provide a Shipper's Export Declaration (SED). The SED is a confidential Census Bureau document, and U.S. exporters are prohibited by U.S. law from disclosing it. As a result, some $70 million worth of U.S. goods were unable to clear Kazakhstan Customs. We were contacted by more than 25 U.S. companies whose shipments were either being held by Kazakhstan Customs or who were reluctant to ship because they had heard of the problem. The U.S. Embassy in Astana, the U.S. State Department, and the Department of Homeland Security's Bureau of Customs and Border Protection, together with the Department of Commerce, repeatedly met with, and sent letters to, Kazakhstan government counterparts in Washington and Astana to urge resolution of the issue. By the end of November, the Kazakhstan government enacted an amendment to the Kazakhstani Customs Code that deleted the section requiring importers to provide a Shippers Export Declaration in order to clear customs.

Commercial Disputes

Our approach is different when a U.S. company brings to our attention a problem that involves a commercial dispute with a local private-sector company. Our overseas teams of experts operate based on guidance found in both the Commercial Service Operations Manual and the State Department Guidance Cable regarding "Assistance to American Citizens Involved in Commercial, Investment, Trade and Other Business Related Disputes Abroad." First, our policy is that support for U.S. businesses and investors operating overseas is a top priority for all U.S. trade agencies. We encourage our team to meet with the U.S. company and the foreign company to provide assistance appropriate to the circumstances. We work with the U.S. company to help facilitate resolution of the issue.

Once a case enters the foreign court system, our ability to help the U.S. company is reduced. We can provide a list of local attorneys compiled by the Embassy, share information about the judicial system or possible dispute resolution procedures, and provide information about how to contact host-government officials who can be of assistance.

Of course, in commercial disputes, the U.S. Government cannot provide legal advice or act as an agent of a U.S. business. Our objective is to ensure that U.S. companies' issues are promptly and fairly resolved. As a general rule the U.S. Government does not intervene in the judicial process of foreign governments, in this instance commercial disputes.

However, our overseas staff can mention the dispute to local officials and the American Chambers of Commerce without commenting on the merits of the case. U.S. business associations will often raise U.S. company problems with local officials, which can have an impact as local officials do not want their region to be seen as hostile to business investment.

Global Nature of Disputes

Companies encounter problems with governments and with their private-sector counterparts in every country around the world, including the United States. The nature of the disputes varies by location. In Mexico, our commercial officers report that the most common type of assistance they give U.S. companies involves payment disputes with local Mexican companies – this is also reportedly the biggest problem that Mexican companies face with each other. In Brazil, our officers report that the most frequent problem that U.S. companies raise with us is their goods being stuck in port because of the complex Brazilian customs and taxation regime. In India, U.S. companies report having the most problems with the regulatory and general bureaucratic system, and Indian companies report the same problem.

In China U.S. companies face, for example, difficulties because of inconsistent regulatory interpretation, as well as lack of transparency in the development, adoption, and execution of certain rules and regulations. Many Chinese authorities are reluctant to offer guidance on certain

requirements. Furthermore, many Chinese laws provide substantial discretion to administrative authorities.

Since China's accession to the World Trade Organization in 2001, IPR, transparency, and other issues have seen marked improvements. However, further improvement is needed in IPR and other areas. The U.S. government is looking to further encourage developments in such areas as the anti-monopoly law that will help improve the business climate for U.S. firms. We use our two primary economic dialogues with China, the U.S.-China Strategic Economic Dialogue and the U.S.-China Joint Commission on Commerce and Trade (JCCT), to address our concerns about China's business and investment environment and to resolve specific concerns.

Being Proactive in the United States

The most important thing we do in addressing any type of business issue is to be proactive. This involves educating and counseling U.S. companies about local business issues and working with foreign governments to effect changes to make their commercial environments more hospitable for all companies. We urge U.S. companies to study export markets in order to have a strong understanding of both the opportunities and the challenges—this due diligence is essential.

There are a number of ways we try to ensure that U.S. companies are aware of potential business issues in foreign markets. First, the trade specialists in our 107 domestic offices are trained to address the kinds of issues U.S. companies face. They conduct local outreach and seminars to the U.S. business community and cover both the opportunities and challenges of entering foreign markets. They also conduct individual counseling sessions with U.S. companies – we estimate that over 100,000 such sessions took place last year. When involved, U.S. Commercial Service trade specialists are able to provide counseling early in the export strategy process to give companies a better understanding of a foreign country's rules and regulations, how to capitalize on them, how to comply with safety and security regulations, and how to jump over exporter hurdles, such as shipping logistics, financing, payments, legalities.

U.S. Commercial Service offices help prepare Country Commercial Guides for specific countries, which is the U.S. Government publication that U.S. companies principally turn to before going overseas. This guide has a section in the first chapter on "Market Challenges," which outlines the problems about which U.S. companies need to be aware. It also includes an Investor Climate Statement, prepared by our colleagues at the State Department.

U.S. companies can easily access a number of resources by calling the Trade Information Center's (TIC) toll free trade help line at 1-800- USATrad(e), to speak to regional experts, or be referred to any of the 107 U.S. Export Assistance Centers nationwide. The TIC also conducts webinars, on such topics as*: How the European Union Chemical Regulation May Affect Your Company* and the *New Automated Export System Requirements.*

We now have three region-specific business information centers (China, the Middle East, and India) to support the efforts of U.S. companies in these regions. Each information center is staffed with regional experts and has a web site linked to *Export.gov* with the latest market information, including sections on problems companies are likely to encounter in those markets.

We are also leveraging partnerships with private sector providers through our Corporate Partnership Program to educate more U.S. companies about doing business overseas. For the past five years, we have hosted seminars throughout the United States educating companies about the challenges and opportunities of doing business in China. For instance, two years ago we conducted a "Doing Business in China" seminar in Ohio which drew more than 1,000 attendees. For several years, we have participated and counseled companies at the "Asia Business Conference" at the University of Southern California Marshall School of Business. Last fall, we did a seven-stop seminar series with PNC Bank called "China Smart Roadshow." These seminars featured our Senior Commercial Officer based in China and included presentations on risk management and getting paid, how to evaluate Chinese partners, and tactical considerations for IPR protection. In all, the two week series reached more than 900 SMEs.

Our Trade Compliance Center (TCC) regularly provides training to U.S. officials in the field and at headquarters on methods to identify foreign trade barriers and produce results that gain market access for U.S. exporters and investors. Throughout the year, the TCC conducts outreach activities to raise awareness of ITA's Trade Agreements Compliance Program among U.S. firms and identify firms that have encountered foreign government trade barriers to market access abroad. This outreach includes counseling companies at trade shows, association meetings, and individually to ensure they are aware of the program and their benefits under our trade agreements. In addition, other important outreach activities include:

- The **TCC Website's** online resources include: an online complaint form for public inquiries and complaints about foreign trade barriers, the texts of over 270 trade agreements between the United States and its trading partners, exporter guides that explain in easy to understand terms the most important agreements, and links to other U.S. Government resources.

- The **Compliance Liaison Program** is an outreach effort engaging the members of trade associations, state industrial development organizations, Congress and other members of our Compliance Liaison Program, and soliciting the assistance from our Commercial Service domestic field offices and overseas posts to proactively identify instances of foreign governments' potential non-compliance with U.S. trade agreements. Every Member of Congress has identified a liaison to the Department of Commerce for this purpose.

Being Proactive – Internationally

When U.S. companies arrive in a country to do business, they often seek out U.S. Embassy officials, including our Commercial Service staff. The embassy team often provides a briefing on the unique issues the company will face in the market. Last fall, the Commercial Service launched the Transformational Commercial Diplomacy initiative, which shifts some resources from well-developed markets, such as France and Germany, to rapidly growing emerging markets where U.S. companies are more likely to need our assistance such as Brazil, China, and India.

The Department of Commerce coordinates closely with other U.S. government agencies to work with foreign governments to improve their business environments. For example, the JCCT has made significant progress in helping resolve software piracy issues as the Chinese agreed to preload legal operating system software on all computers produced or imported into China. We also have Commercial Dialogues, government–to–government meetings on issues raised by each country's private sector, with Russia, Brazil, and India. The Commercial Dialogue with Brazil helped to improve the express shipment process within Brazil, which has partially addressed the customs problems U.S. companies encounter.

Senior Commerce Department officials often travel to countries where U.S. companies are experiencing problems consistent with a lack of a rule of law. In such countries, we often raise the need to develop a predictable and transparent legal system to our foreign government counterparts in order to create a more inviting business environment and encourage international trade and investment.

The Department of Commerce's Commercial Law Development Program (CLDP), provides technical assistance to foreign governments on developing a transparent and open commercial legal system. The CLDP trains judges and legislatures in these countries on various subjects from how to write regulations to setting up alternative dispute systems. Countries where the CLDP has recently completed training programs include: Algeria, Jordan, and Tunisia.

Conclusion

In conclusion Mr. Chairman, we have a very robust system for helping U.S. companies when they have problems overseas. We are focused on assisting them with current issues and working hard with foreign governments to prevent problems from occurring in the first place. We have positioned both our overseas staff and our policy focus towards addressing the most common problems U.S. businesses face in the markets where we are most needed.

Our goal is to enhance the U.S. companies' international experience and success so that exporting becomes an integral part of their business - ensuring that U.S. exporters are well-versed in the rules, regulations, trade opportunities and business culture of the target countries

and regional markets to take advantage of changing markets and to avoid exporting missteps that may affect their companies' bottom line.

Mr. SHERMAN. Thank you. Mr. Nelson, has the U.S. Government done anything with regard to the Arbitrator Wang Shengchang, who ruled for an American business in Stockholm, and then was in prison?

Mr. NELSON. Mr. Chairman, I am sorry. I am not familiar with that specific case. I will look into that one, and we will get back to you with an answer on that.

Mr. SHERMAN. It strikes me as instructive that when a Chinese arbitrator is in prison just after ruling for a U.S. company, that is so commonplace, so consistent with expectations, that it just gets lost in the shuffle.

Mr. Nelson, in allocating resources, do you differentiate between those companies that are just trying to exploit the U.S. market that are offshoring jobs to bring things back here, and those that are trying to conduct business with consumers in the other country; exporters versus importers? Are they all equal?

Mr. NELSON. Sir, our policy is to assist all American companies that seek our assistance.

Mr. SHERMAN. So they are all equal?

Mr. NELSON. We do not turn away any American citizens coming to us.

Mr. SHERMAN. But you do not prioritize the exporters over the importers; or the importers over the exporters; or the left-handed over the right-handed?

Mr. NELSON. We are open to provide assistance to every American citizen.

Mr. SHERMAN. Okay, so we do not really care about the trade deficit or jobs for Americans. We just want to make sure that our corporate sector is treated well; and the U.S. taxpayers in my district will pay for that process.

Now you do issue these reports. But, you know, the long report, it is hard to compare one country to another. Do you rank or categorize countries in terms of their fairness to U.S. business?

Mr. NELSON. To my knowledge, we do not do that. What we do is, we publish these investment climate statements with the view that a company looking to invest in a particular country would analyze carefully the investment statement, the situation in that country.

Mr. SHERMAN. But the question will often be, compared to what? Then the other issue is not just providing information to companies. It is pressuring the countries.

We have the largest trade deficit ever. China can create a circumstance where we have no access to its markets; just by mistreating our companies. If we do not rank China, then they are free, and other countries are free, to do whatever they want.

I would hope that you would issue categorizations; and that your categorizations would focus on how companies are treated when they try to exploit the local market.

Because you see, it is easy. If I want to be an importer, I can read your country report on China and say, Oh, not so good. I will go have my goods manufactured in Vietnam, or some place else where you suggest.

But that is fine if you want a $7-, $8-, $900-billion trade deficit; maybe $1 trillion trade deficit. What if we wanted our companies

to exploit the local markets, to sell U.S. goods there? That is obvious. You cannot go to Vietnam in an effort to sell goods to China.

Now Bush is going to the Olympics. Was your Bureau consulted as to whether China treats America fairly; and particularly, whether it treats its arbitrators fairly when they rule in favor of Americans, in deciding whether Bush should go to China?

Mr. NELSON. Sir, the issue of economic relationship with China is very high on the agenda of the administration. It is something that has been looked at very closely.

I was not directly consulted about the President's travel plans. But the President is certainly aware of the JCCT negotiations that my colleague discussed. He is aware of the SED discussions that Secretary Paulson shares.

Mr. SHERMAN. But he is certainly not aware of the arbitrator who is in prison now. The entire Olympic Games are paid for by intellectual property right protections in the United States. All the money for that is coming from our broadcasters, our sponsorships.

Yet, you walk down the streets of China, and what you see if the exploitation of U.S. intellectual property. They are selling the disks there on the streets before they are released.

Apparently, this irony was never brought to the President's attention. He is going to a giant party, paid for by American intellectual property, in the heart of the place where they rip off American intellectual property.

I would hope that in the future, your bureau has a very strong role in shaping American foreign policy. Some day, we will care about the trade deficit. We will care about jobs for Americans. We will not just care about whether the President gets to see the basketball game. I now yield to Mr. Royce.

Mr. ROYCE. Thank you; let me begin with an observation, Secretary Nelson. The State Department issues travel warnings to Americans, telling them about the risks overseas. I would ask, have you considered issuing formal investment warnings?

Mr. NELSON. Sir, we believe that the investment climate statements that we issue for each country serve that purpose.

Mr. ROYCE. And in it, you said that the Chinese court system is incapable of guaranteeing the sanctity of contracts. But it seems to me that in order to get this to a level where people take notice, an investment warning, especially given the number of cases that we are hearing about from our investors, from U.S. investors attempting to do business in China, that might be a way really to make that point.

I wanted to ask sort of a related question to you, Secretary Hernandez. Because you testified that the Commerce Department has held numerous conferences on doing business in China throughout the United States.

Well, that is how a number of individuals have been brought to focus on that investment market; and on the second panel, we will hear from one business woman who had a nightmare experience in China. But, of course, as you know, she is not alone.

So are you confident that these conferences provide a sufficiently realistic picture of those land lines that many investors confront, when they go to China? The State Department offers a very somber assessment of corruption, if you dig deep, and a lack of rule law

in China. Are you concerned about the way these are presented; about leading American businesses astray?

Mr. HERNANDEZ. Well, Congressman, I can tell you with confidence that our trade specialists do not sugar coat the scenario; not just in China, but with all the markets moving forward.

The first thing that we do in a seminar or outreach program, is that we tell every company, based on your own level of risk and appetite to do business overseas, you have to be informed as to how you enter and have a realistic approach. Every trade specialist under the Department of Commerce—whether it is domestic or overseas—very much provides the landscape.

We do not just provide the opportunities. We very much highlight the challenges that exist in all the countries around the world; not just China.

Mr. ROYCE. Well, let me go back to Secretary Nelson. On the next panel is Nancy Weinstein; Nancy's Lifestyles, was her company. She will testify about the frustration she has felt that the U.S. Consulate in Shanghai has not filed a complaint with the Shanghai Foreign Investment office regarding her dispute.

Chinese authorities have cited this to her as an omission; and I know that you are familiar with her case. She will testify that quoting, "Waiting until 7 months later, lost its impact, and a complaint has yet to be filed."

Would you fill me in the State Department's thinking on that score?

Mr. NELSON. Yes, sir; yes, I am familiar with the reporting from Consulate on this difficult case and unfortunate matter. Certainly, it is something which our Consulate has been involved, I believe, from the very beginning. I understand the Consulate General was actually present at the opening of the facility, and has been in regular contact.

Mr. ROYCE. Right, we understand; they were opening up the facility of her store. Because this was a considered a pretty major investment in Shanghai.

Mr. NELSON. Right, and my understanding is that there have numerous contacts, consultations with Ms. Weinstein between the Consulate, including the commercial service officials present there. We have raised it with the local investment. I am not sure exactly which investment authority, but it was certainly with the investment chambers. We brought it to their attention.

We have made the point to them that as they seek to attract investment in Shanghai—which is their policy to attract investment. These kind of cases, if they are not fairly and appropriately handled, risk alienating further investors. We have made that point to them, and I believe that they fully understand that.

Mr. NELSON. Well, in this case also, besides not filing a complaint with the Shanghai Foreign Investment Office, we had a situation in the case where the U.S. commerical service and Shanghai declined to send a representative to her March 19th court proceeding, because to do so "might be considered as interference with the Chinese judicial system."

Now as we learn more about the lack of a Chinese judicial system in these cases, that is certainly an interesting quote. But those were the words from the U.S. Consulate.

So you had testified that in the past, and subject to staff availability, Commerce and the State Department officers have sat in as observers at court proceedings.

Does "in the past" mean that this is a past practice, no longer in effect; and what was the thinking again, in this particular case, in not attending the Court proceeding?

Mr. HERNANDEZ. Actually, I think I will answer that question. Our conversations with Ms. Weinstein have been throughout months. We have had several phone calls, making sure she is aware of the whole judicial process.

It is correct that we suggested it best that we not attend this hearing with her; also, highlighting the fact that we do not want to undermine the independence of our own judicial system, even though we know that it lacks transparency and it is unpredictable. We know exactly from the Web sites and all the briefings that we have given other companies, as well.

So we have very much tried to offer as much assistance as possible. But to go and be present in a hearing that is part of this process is something that we do not do, by policy.

Mr. ROYCE. You know, I have got to tell you, I personally testify to the rotten nature of the Chinese courts. Personally, I am not all that concerned about playing with such self-imposed restraints.

It seems to me that a little transparency might be helpful when you are dealing with this level of corruption. So I just have to confess, I do not quite understand the perspective. I mean, if you had a functioning judicial system, I would. But absent that, it is beyond me.

Mr. HERNANDEZ. Well, Congressman, one of the things that we do is, we do provide information for every business person who goes to China, or to India, or to Russia. I mean, this is not just endemic to China.

Once again, our policy, consistent through all the cables that have been sent out from the State Department to all those at Embassies and posts, means that we do not interfere with the judicial process.

There are attorneys who can actually go and support, as they go through the judicial process in China, and in India, and in Russia. But for the most part, we very much work under the conditions that we are not going to interfere into the judicial process of any other country; much like we would not want them to interfere in ours.

Mr. ROYCE. You know, assemblism in China, and U.S. pressure is lacking. Again, you are talking about court systems that function in the West; and then you are bringing up Russia and China, where there is a lack, where there is an implosion and a corruption that undermines the effectiveness.

If you wanted to help the people in China, one of the key objectives would be to get a functioning court system with independent judges, who were actually making decisions on the part of Plaintiffs making decisions on the basis of the rule of law; rather than on corruption, and the same goes for Moscow.

To avoid doing that and the whole equivalency argument, the absence of any functioning legal system in these types of cases is something I just do not follow.

Mr. HERNANDEZ. Well, Congressman, I, too, share your frustration; because it is widely known about the system.

Mr. ROYCE. Listen, if it is widely known, then we should put out those formal investment warnings to U.S. business people, so that they know the real state of affairs. That is my complaint. We need a little bit of honestly, all the way around.

I think it will help the people in China if we get a little honesty on these issues. I would hope it would help the people in Moscow.

But it is about time that we quit pretending about the existence of a legal system operating with a concept of trying to achieve justice in these situations; especially given the amount of looting that is going on in this environment.

Mr. HERNANDEZ. This weekend, on my own, I did my own queries on different Web portals; and put U.S. exports, trade to China, how to do business in China.

The great thing about what surfaced is that every page, the Export.gov Web site sponsored by the inter-agency and Department of Commerce surfaced as one of the top three Web sites to leak.

When I look to China—which is not the only country I looked at—when you looked at the pages that we list, there are four bullets that we list: How to avoid scams in China; how to protect our property in China; how to do business in China; and the first sentence that we list is, American companies have mixed experience in China.

It is a country that its current legal system and regulatory system can be opaque and consistent, and often arbitrary. We very much highlight how it is to do business in China. We do not just highlight the opportunities.

Mr. ROYCE. Well, let me close with this. We hope China's legal system develops. But let us have pressure, because I do not think the Chinese understand our absence on this front.

I do not think they comprehend fully why we would not issue those formal investment warnings and broadcast them to potential investors; nor why we would not weigh in and send to some of these proceedings, you know.

Our investors are told, look, do not show up for the case, because if you do, you run the risk of being arrested in China.

Mr. HERNANDEZ. Exactly.

Mr. ROYCE. I mean, they are given that message. It would be nice if they had a little assistance, since they are facing possibly, after being fleeced, hauled off to a Chinese jail. So I will just let you continue, Mr. Chairman.

Mr. SHERMAN. I will point out that warnings might be useful. But warnings alone are a way to achieve $1 trillion trade deficit. Because we would just never have access to the Chinese, if they are able to discriminate those of our companies that are trying to exploit their market; and our response is to have a big red light saying, well, do not invest there at all.

Mr. HERNANDEZ. At least invest with a full knowledge of how to do business there.

Mr. SHERMAN. No, it is not that American companies are not smart or knowledgeable. It is that American companies are screwed, and their government will not take up their case.

Their government has made it clear to the Chinese that we will give total access to our market, no matter how they use various devices to screw our companies that are trying to exploit theirs. Do not blame the companies for not reading your books. Blame the U.S. Government for the trade deficit.

Mr. HERNANDEZ. Mr. Chairman, you should not blame the government. Because when you look at the resources we provide, every company has an opportunity to decide, I am not going to——

Mr. SHERMAN. The question is not the companies.

Mr. HERNANDEZ. Exactly.

Mr. SHERMAN. The question is the trade deficit. Read your books. You get a choice. Go to China, and you get screwed. Your government will not help you; and with total access to U.S. markets, we will be available to China, no matter how bad you get screwed.

Do not go to China. Take our warning seriously, and watch that trade deficit go to $1 trillion. But do not worry. That is just manufacturing jobs. That is not jobs in Washington, DC. I yield to the vice chairman of our committee.

Mr. SCOTT. Thank you, Mr. Chairman, and to continue that line of thought on China—— [Applause.] I trust, Mr. Chairman, that applause was for you, Mr. Chairman, and not for me. [Laughter.]

Mr. SHERMAN. No, it was for the gentleman from Georgia. It happens every time he appears.

Mr. SCOTT. I join you in your very thoughtful and insightful analysis of the situation. I want to carry it on a little further. Let me just ask you, Assistant Secretary, does China engage in counterfeiting copyrighted, patented, trademark goods?

Mr. HERNANDEZ. Yes.

Mr. SCOTT. How serious is that?

Mr. HERNANDEZ. It is very serious. We have drawn attention to it. It is absolutely one of the discussions that we have, which is necessary with China. But it is not just China alone when you raise this issue. There are other countries that we work with and have this conversation with.

Mr. SCOTT. Does China engage in currency manipulation?

Mr. HERNANDEZ. Any issues related to the currency really need to be directed to the Department of Treasury. Because I do not work with currency issues.

Mr. SCOTT. Well, what is your opinion on the matter?

Mr. HERNANDEZ. I am not here to give my opinion. I am here to provide information about trade.

Mr. SCOTT. All right, does China engage in unfair subsidies?

Mr. HERNANDEZ. That is an issue that USTR is dealing with.

Mr. SCOTT. Okay, how would you answer this question? Is the growing trade deficit with China the result of unfair trading practices on their part?

Mr. HERNANDEZ. With respect to our trade with China, it is very dynamic, in the sense that we are the world's largest economy. We are also the world's largest consumer. We buy more than anybody else around the world. The purchasing ability of our consumers is deep, compared to many other countries around the world.

China is also the fastest growing economy. So you are going to see trade between both of our countries. The most effective way to deal with the imbalance is to have more U.S. exports that move to

China and be sold in China, as they have a growing consumer class.

Mr. SCOTT. One of the areas that I am concerned about are reports of a lack of agency coordination and adequate resources. Do either of you feel that U.S. agencies who are involved in these issues suffer from a lack of coordination, inadequate funding, inadequate staffing or training; and if so, what can be done to remedy the problems?

Mr. HERNANDEZ. I think the issue, or at least the report you might referring to is something that was done by the GAO in 2001. I can tell you that, to date, in the past 6 or 7 years, every single year, we have added more and more resources and experts in China.

With respect to the Department of Commerce, it is now our largest office and presence overseas. We have over 140 people from Commerce relating to Patent and Trade's IPR issues market access issues, dealing with standards, trying to help companies, trying to deal with issues with market entry.

So more than ever before, we have more people. It is more coordinated, because we now are working with more agencies on these particular issues; not only through the JCCT, but the SEC, as well.

So I can say honestly that we are more coordinated. We do have more people there. We are trying to make sure that we help educate and inform and support companies; not only just in China, but in other parts of the world, even before they leave.

Last year, we had 100,000 export consultations with companies about markets that they are choosing to enter, and many were about China. Many were trying to get an understanding. They get so much attention from the media about China, about India. We try to make sure we can offer as much as we can, so that they have as much information as they can before they enter any market outside of the United States.

Mr. SCOTT. Would you say that China is the most problematic nation in which we are dealing with, as far as American business and investment abroad?

Mr. HERNANDEZ. It is really respective to the number of countries going to these markets. We do see a huge number of companies trying to enter China to date. At minimum, we think there are about 10,000 companies from the United States, trying to do business in China. I think the number is growing.

We have more and more companies actually exporting and trading with China. That number is going up. But let me just say one final thing. The newest members to the WTO, if you list them, are the ones that we are really trying to work hard to make sure we have a more predictable environment through our economic engagement.

The newest members to the WTO are China, Vietnam, Russia, Saudi Arabia. These are countries, if you looked at every single one that I mentioned, that have an unpredictable judicial system, and incomplete process of transparency.

So these are issues we are trying to deal, not just with China; but investors are making very aggressive moves toward these other markets as well. We are trying to make sure that we very much have an engagement to deal with these issues.

Mr. SCOTT. Both of you could comment on my final point. We label our discussion this morning with a beleaguered firms. I mean, how serious is this problem? Is it of a crisis nature? Beleaguered is a unique and fascinating word.

Mr. HERNANDEZ. Yes.

Mr. SCOTT. It means they are deluged with problems. If I could get, for the record, what are the most serious problems? What are the complaints? What are the most serious complaints and difficulties we are hearing from businesses and investors?

Mr. HERNANDEZ. Well, you know, we have very good discussions with the business community to get a real idea of what their biggest challenges are, moving forward. I can go from country to country and talk to you about this. But if you just want to focus on China, again, you know, when you look at China——

Mr. SCOTT. Well, I do not want to just focus on China. I would like to get a purview of the landscape; but certainly China.

Mr. HERNANDEZ. The fundamental root causes that concern the community is, as these countries have entered into the WTO, which I listed again—Vietnam, China, Saudi Arabia, Russia—there is a fundamental lack of technical expertise in the country.

You have to understand, these are countries who never operated in a market economy; who never had a judicial system that is relevant to consistent to the Western standard. Now all of a sudden, we are asking them to create everything similar to what we are.

It is moving. I am not going to defend China. But the point is, they are having to learn how to incorporate a judicial system.

One of the programs that we have today with China is a commercial law development program; which is, we are sending judicial experts from the United States to China throughout the provinces and, in turn, they are coming here.

The theme for this year of our commercial law program is patent law, because it deals with one of the big issues of IPR protecting; reminding them what is it of historical, how to proceed in the judicial system, and some of the findings that we use here in the United States. That is just one issue.

But again, you are talking about a country whose regulatory system has not kept up with the hypergrowth that it is experiencing. Oftentimes, we do inform companies that that is the case. We want to make sure that everyone is very informed where every country stands as they evolve and they move. They certainly are like the United States, and we want to make sure companies know that.

Mr. SCOTT. Thank you, Mr. Chairman.

Mr. SHERMAN. Thank you; it is amazing how quickly China has learned to exploit our market, and how slow they have been to learn how to treat our companies fairly.

With that, let me introduce members in the order in which they came. I believe that is first, Mr. Tancredo from Colorado. Oh, he just left. Well, he was here first. [Laughter.]

Mr. Poe from Texas.

Mr. POE. Thank you, Mr. Chairman; I have a question for each of you, but a comment on China. It is interesting. It seems like our Government goes out of the way to never mention the phrase, Communist China. I do not know why that is.

I mean, I was in China in the 1990s, and as a former judge, I saw their system, and I do not call it a judicial system. It is just a system. I was not impressed with their system at all as far as fairness.

But be that as it may, is there some government, is there something in our administration that sent some edict out to the hinter lands—do not mention the words, Communist China? I am not afraid to say that China is Communist. We just never hear that phrase.

I have got two questions, and thank you for being here, Mr. Hernandez. The last time we were here, we talked about South Korea.

Mr. HERNANDEZ. Yes, sir.

Mr. POE. And it had to do with issues of rice, and I am going to talk about rice today. I asked you a question then. The question that I asked you then was from the Texas Rice Federation.

You did send me a reply. But part of your reply, and I have it here, suggested that I contact the Rice Federation in answer to the question. So I am a little confused. Maybe we should follow up on that.

Mr. HERNANDEZ. Yes, sir.

Mr. POE. The issue is Japan. As you know, Texas rice farmers—and I represent almost all of them from Liberty and Jefferson County—used to have a pretty good market. But history has been unkind to the rice farmers. Their number one trading partner was Cuba, and then Iran, and then Iraq—bummer. [Laughter.]

Now they are trying to go other places. South Korea is one of those, and we will talk about that privately, because we have other things to talk about.

But Japan now is one that they are concerned about, as well. As you know, Japan has an agreement that they will take so much rice from the United States. They have not lived up to that agreement. They are not getting the minimum quota as they have agreed to do.

When they get rice from us, they stockpile it and do not use it. They go ahead and have the free market of Japan rice in Japan. That has been going on for some time. I want to know what we are going to do about that. We want to sell Texas rice to Japan.

Mr. HERNANDEZ. As you should; and sir, let me get back to you on that. I will make sure that I confer and work with my colleagues within the International Trade Administration, focused on Japan and this particular agreement, and why they are not meeting their quota.

Mr. POE. Well, I know you are aware of the agreement; and they have now repeatedly, year after year, made it more difficult. But bottom line, they are not living up to their agreement, and we need some help. Because we have a WTC agreement with them, and we want to sell rice to Japan. I know that sounds ironic; but we want to do it. Texas rice farmers have long grain rice, as you know; and so we need some answers on that.

Also, I want to talk about, Secretary Nelson, this is a long ongoing problem. There is an insurance company in Texas called TIG. TIG made a contract with an Argentina insurance company, years ago—the Argentine insurance company in Caja, C–A–J–A.

The Government of Argentina restructured Caja during the 1970s, privatized the domestic business, and assumed the debt of foreign investment. That was in 1970 through 1990.

The EIG has asked for that money that has been owed them now for 18 years, for our Government to help get that money back. It is about $15.7 million, with a fine of $2,000 a day from one of our District Courts.

I have a letter here on July 28th, 2005. Secretary Rice was contacted by the chairman of the Foreign Affairs Committee, Henry Hyde—God rest his soul—asking what our Government is doing.

I have got a letter, October 2005, from Ranking Member Patrick Leahy—what is our Government doing to get this money to this little Texas insurance company, TIG?

I have a letter, September 2006, to the Secretary of the Department of Agriculture, from two Texas representative, Kay Granger and Henry Bonea—what is our Government doing? Of course, the Agriculture Department relied promptly, it is not our problem. It belongs in the State Department.

The second letter is from Kay Granger in 2006 to the State Department, asking what is taking place. Finally, in April of this year, I sent the new Ambassador from Argentina, asking what is taking place. Basically, we have not gotten an answer.

So it is $15.2 million; what are we doing? It is an 18-year-old debt, under anybody's system. Our Government ought to be able to do something in 18 years. [Laughter.]

Mr. NELSON. Sir, I am not familiar with that letter. I am surprised the Members of Congress did not receive answers. I will look into that. They certainly deserve answers.

In terms of specifically what is going on in helping that company to collect its debt, I will have to look into that. But I will certainly get back to you.

Mr. POE. Well, the overall question is, there are two Federal judgments in District Courts on each side of the United States, ordering this payment. So there is Court action on this.

But another question is, why do we keep doing business with a country that will not pay their debts; even if it is a little bitty Texas insurance company? That is the second question. Why do we do that? Why do we keep doing business with countries that do not pay their debts to private companies?

Mr. NELSON. That is certainly a decision that companies need to make when they go into business in Argentina and any other country; the risks that they face. That is a decision that the companies have to make, as to whether the risk is worth the reward. In the case of Argentina——

Mr. POE. No, that is not the question. The question is, this decision was made in 1970 to do business with Argentina. Argentina socialized the company; agreed to pay off the international debt in 1991. My question is, why do we, as a nation, still encourage business to a nation that does not pay off lawful judgments and debts to American companies? That is the question.

Mr. NELSON. Sir, we are seeking to get Argentina to comply with arbitrarial awards in some other cases that I am a little bit familiar with. According to my information, it does not list TIG as being part of that.

But in similar cases, there was an international arbitration decision that Argentina was subject to, where Argentina lost and was required by the arbitral Court to pay. They have not made that payment. We are very concerned about that, and are pressing to make the payment.

In those cases, I do not know if the TIG case is similar to that, or a party to this one. I will look into that. But the need for Argentina and other countries to comply with the international obligations is certainly something that we are very concerned about; and we press them on a regular basis. We press them as best we can to implement those decisions.

Mr. POE. The Northern District Court of California has ordered a $2,000 fine per day for failure to pay a lawful judgment. It just keeps being ignored; and like I said, after 18 years, you would think that somebody would get their attention.

Last question, do you know of any policy written, Mr. Nelson, in your department, where you are not supposed to refer to China as Communist China?

Mr. NELSON. Sir, I am not familiar with any policy like that. I think that our normal reference of People's Republic of China is the title we use.

This kind of goes back to an observation that other members of the committee have made before. The important policy in China is that they move to adopt global standards of justice, global standards of contract enforcement, global standards of intellectual property protection; that they move away from the arbitrariness of the system that they had for many years there, and it is still an incomplete process. They have not completed that transition.

We very much are urging and pressing and working with them, to bring them into the modern global economy, and move away, whether entitled or not, from the system that they had.

They are in a transition to capitalism. They are in a transition to a market economy. Hundreds of millions of people in China have come out of poverty, because of the transition that started some two decades ago. We are certainly encouraging that, and we are encouraging them to move any political transition at the same time. That is equally important.

We are engaging with them in numerous ways, including through not only economic engagement; but through high level discussions all the time, pressuring them to move into that modern economy.

Mr. SHERMAN. Thank you both; I would point out that at least I stopped calling them Communist China. Because it is not necessary to distinguish them from Nationalist China, because the folks in Tai Pae have pretty much stopped claiming to be the government of the entire country.

I never called it Communist Cuba or Communist Vietnam. But we all know that it is a regime run by the Communist Party, which may or may not still believe in Communism.

Mr. POE. We certainly do not want to call them Red China. Because everybody will think they are a bunch of Republicans over there. [Laughter.]

Mr. SHERMAN. The cozy relationship between some members of your party and the government of Beijing will not be commented upon. [Laughter.]

Let us recognize the gentleman from Arkansas.

Mr. BOOZMAN. Coming from Arkansas, first thing, I will agree with him on selling rice, I think we are perhaps the leading rice producer in the world.

But I want to thank you all. I have had the opportunity to work with both of you all, you know, and especially Mr. Hernandez. I get frustrated seeing all of these containerships coming here, you know, filled to the brink and going away empty.

So we have worked really hard in our district, you know, to try and turn that around. I think with your efforts, we are having success in doing that.

The problem though is that as we do that, then problems arise. I know in my district, I can give horror stories of people dealing with Russia, that have not gotten paid. People in South America, China, you know, horror stories; and then also, places like the U.K., in the sense of individual businesses.

What I would really like for you to consider, you know, the world is so different now than it was 5 or 10 years ago. We are very rapidly moving to a cash-less society.

I had an individual that had a small computer company, sold it to a business supposedly in the U.K. They received the payment. They paid by credit card.

She waited until it was deposited in her bank account. You know, she sold the stuff, and it turned out it was a phony credit card. Then they actually yanked the money out of her account, you know, and were able to do that in some way.

So I guess what I would like to see is, some of this stuff, we really need to look at the current legislation that we have—you know, the current protections. I do not know if those type of arrangements are treaties or whatever. But even in valid situations that we all take for granted, there are lots of situations arising now.

I had a question about one of the ways to perhaps coerce folks, countries, into being a little bit more cooperation; which was the ability to not give them visas, you know, for students and things.

Is that a consideration at all, Mr. Nelson? Is that kind of a tool in the tool box that could be used? I really like students coming here. That is the other problem, you know.

Mr. NELSON. Yes, Congressman, the visa issuance is something that is generally considered a positive thing to bring people into the U.S.

There is Section 225 of the Formulations Authorization Act, which does permit the application of visa policy to certain cases, but under very restricted conditions.

Basically, it says that the Secretary of State has the authority to make a determination of visa ineligibility for an alien who, through abuse of an official position for personal gain, inverts or is complacent in a conversion of confiscation of appropriated real property owned by a U.S. national. So it is focused on abuse by government officials of their official position.

Mr. BOOZMAN. Very good; again, I would appreciate, like I said, you know, at some point, your staff giving us some information. I

think we are starting to turn the corner a little bit and be successful in some of these areas.

But as the commerce increases—and again, I am not talking about us setting up shop. Although for those companies that want to do it, you know, that is fine; where they manufacture. Then you run into things like protecting their products and that sort of thing.

But very much, we are starting to sell a lot of products overseas. Yet, we need to have the ability, you know, somehow to ensure payment. That is really where the conflict I see arises so much; that companies just do not pay.

Then, again, as I mentioned with the credit card thing, this scam happened to come out of Nigeria. That is a huge problem there. We could talk about that; and they probably did more damage to the system, or as much as anybody else, because of this type of fraud that is pretty sophisticated. So again, like I said, I hope that you can work with us in those areas; thank you.

Mr. ROYCE. Will the gentleman yield for a minute?

Mr. BOOZMAN. Sure.

Mr. ROYCE. In the Nigerian case, I know that Section 225 was then applied. It was applied against Nigerian nationals.

I wonder, in this case, do you have Communist Party members, whose families want to come here as students; but who are involved in oversight basically, as government officials, of the party?

They are the ones that are not reforming the judicial system. Their children and grandchildren, their relatives, come here to universities. It is a highly sought-after position. They say this was applied in Nigeria as a consequence of just fraud. I remember the case.

So I think it could be applied by the State Department to China, should it not reform the process. Mr. Nelson, it is something we ought to look at; thank you very much.

Mr. SHERMAN. I want to thank our first panel of witnesses. We may have been a little tough on them. But we realize that they are working hard every day, and that our argument is not with their work, but with the policy set at the highest level.

With that, let us bring up our panel. They include, first on our list, Nancy Weinstein from California, from Orange County, I believe—Long Beach, close enough. She is the founder and CEO of Nancy's Lifestyles, LLC, a home furnishings corporation that exports American interior design through her showroom and through her television show.

I would point out that Nancy, as much as anyone, is the reason for today's hearings. I want to thank Mr. Hernandez for talking to Nancy, because I know this will be first on his list, when he gets back to his office.

Since the experience she had, brought to the attention of our ranking member, really illustrated the need for these hearings and, more importantly, the need for a change in our Government's policies.

Second, we have Jonna Bianco. She is the President of the American Bondholders Foundation, LLC, which represents American families who hold defaulted sovereign-backed bonds that were issued by pre-Communist governments of China.

Finally, we have Alan Tonelson, who is a Research Fellow at the U.S. Business and Industry Council, Education Foundation; and author of "The Race to the Bottom" and "Made in China; America's Failed Trade Policies Toward the People's Republic."

I want to thank you for being here. We look forward to learning a lot. We will start with Ms. Weinstein.

STATEMENT OF MS. NANCY WEINSTEIN, CEO AND FOUNDER, NANCY'S LIFESTYLES

Ms. WEINSTEIN. Thank you; I am Nancy Weinstein, CEO and Founder of Nancy's Lifestyles. I am a professional interior designer. I have been traveling to China for business for the last 14 years; and the past 4 years, my total focus and passion has been to open Nancy's Lifestyles stores in China.

In 2005, I rented a 12,000 square foot building, which I thought was going to be the perfect first store for Nancy's Lifestyles. Instead, it became the worst nightmare of my life.

The landlord and his mafia style actions did everything possible to stop my company from opening. It took 18 months to get the electric installed. He would never turn on the heat or air, and it was over 100 degrees inside the building in the summer. I continued to pay the monthly rent on the advice of our lawyer. I had paid the landlord over $1,100,000 in rent.

Just 3 days before we were to open, he threatened my life and told our lawyer, "If Nancy does not pay him $35,000 in 2 days, Nancy and her friends could get seriously hurt at her opening party."

I paid him the money. I hired two security guards and a bodyguard. My store opened in March 2007; and after 6 months of more constant problems caused by my landlord, I had decided we had to close.

He sent 12 thugs to my showroom, and they told my workers that if they worked for me, they would beat them and hurt them. They would not allow my workers to move out the furniture to the waiting trucks.

They held my workers hostage for 7 hours. We called the local Ji Nan district police, and they would not do anything to help us. I have been told by so many people in Shanghai that the landlord pays off people to get things done his way.

Several weeks later, the landlord broke into my showroom and stole all of our $500,000 in inventory and fixtures and everything from my office, which all belonged to our U.S. company.

Everything is gone. My lawyer and the former Director of the Shanghai Foreign Investment Office went to report the crime to the Ji Nan district police.

The police said, yes, they knew that my landlord had taken everything. The police actually allowed this guy to steal my entire store. He stole my entire business. He has not been arrested.

Now he is suing our Shanghai company for $100,000, saying that we did not pay him enough rent. That is, of course, not true.

It is so easy for him to make false claims with the power and the connections he has. The judge in the case has actually met with the landlord's attorney privately, outside of court. The judge has

not done anything to him regarding his stealing the inventory that belonged to our U.S. company.

Now the furniture is dirty, damaged, and broken. They threw in the trash $25,000 in hundreds of our logo items. He also stole our company files. So we do not have all of our papers to defend our company.

In the last 7 months, I have repeatedly asked the Shanghai Foreign Investment Office in Shanghai for help. After all, the U.S. allows them to bring Chinese Delegations to the U.S. and invite U.S. business people to invest in China.

I did invest in China. They say they cannot do anything to help me. I have brought it to the attention of the Chinese Consulate in Los Angeles, and also the Director of the Shanghai Foreign Investment Office in Los Angeles. He told me he is in L.A., and cannot do anything about what happens in Shanghai. I never received any help from any of these offices about this matter.

I had notified the U.S. Consulate in Shanghai immediately when this all happened. They had a gentleman from the Commercial Section contact me. I was told there really was not anything they could do.

I received no help from anyone until Congressman Royce started looking into what has been happening and this hearing date was set. Then the action started happening.

The Shanghai Foreign Investment Office called me. They were looking for the U.S. Consulate to file a claim against the landlord. The gentleman at the U.S. Commercial Section said they could not do anything without permission from Washington.

Mr. Huang, who is the Director of the Shanghai Foreign Affairs, had asked that I call him. Mr. Huang said it was "nothing" that my workers got pushed and shoved, and threats put on their lives that they would be beaten.

The U.S. Consulate had a meeting with Mr. Huang. He said that he wanted to make a deal, and he did not want me to testify. He said he could get a deal for me to pay the landlord $14,000, and he would forget the case.

Mr. Huang said he asked the landlord if he stole the furniture, and he said no. Mr. Huang said he believed him. The furniture is in the landlord's warehouse, and his own lawyer told the judge he took it. There was no help on the part of the local Shanghai government.

I hope that this will be a good lesson for other American business people who are considering going to China. My story is one of thousands of cases that have happened to other American business people in China.

I personally feel it has become a dangerous place to do business. There are so many greedy, well connected Chinese business guys in China, that pay off the right people and get what they want, and we have no recourse. You can see by my story how bad it can get.

I think if the U.S. Consulate was able to respond immediately back in December when this happened and file a complaint, it would have been helpful. Waiting until 7 months later has lost its impact.

I want to thank Congressman Royce, Chairman Sherman, and the other members of this committee for taking the time to hold

this hearing; and I hope that any American thinking of making an investment in China will think twice.

They are on their own in an unethical environment of payoffs and power, where even the toughest of American business men and women have problems; thank you.

[The prepared statement of Ms. Weinstein follows:]

PREPARED STATEMENT OF MS. NANCY WEINSTEIN, CEO AND FOUNDER, NANCY'S LIFESTYLES

Thank You.

I am Nancy Weinstein, CEO and Founder of Nancy's Lifestyles. I am a professional interior designer. I have been traveling to China for business for the last 14 years and the past 4 years, my total focus and passion has been to open Nancy's Lifestyles stores in China.

In 2005, I rented a 12,000 sq ft. building which I thought was going to be the perfect first store for Nancy's Lifestyles. Instead, it became the worst nightmare of my life. The landlord and his mafia style actions did everything possible to stop my company from opening. It took 18 months to get the electric installed. He would never turn on the heat or air and it was over 100 degrees inside the building in the summer. I continued to pay the monthly rent on the advice of our lawyer. I had paid the landlord over $ 1,100,000 in rent.

Just 3 days before we were to open, he threatened my life and told our lawyer, "If Nancy doesn't pay him $35,000 in two days, Nancy and her friends could get seriously hurt at her opening party." I paid him the money. I hired two security guards and a bodyguard. My store opened in March 2007 and after 6 months of more constant problems caused by the landlord, I had decided we had to close. He sent 12 thugs to my showroom and they told my workers that if they worked for me, they would beat them and hurt them. They would not allow my workers to move out the furniture to the waiting trucks. They held my workers hostage for 7 hours. We called the local Ji Nan district police and they would not do anything to help us. I have been told by so many people in Shanghai that the landlord pays off people to get things done his way.

Several weeks later the landlord broke into my showroom and stole all of our $500,000 in inventory and fixtures, and everything from my office which all belonged to our U.S. Company. Everything is gone. My lawyer and the former Director of the Shanghai Foreign Investment office went to report the crime to the Ji Nan district police. The police said yes, they knew that my landlord had taken everything. The Police actually allowed this guy to steal my entire store. He stole my entire business. He has not been arrested.

Now he is suing our Shanghai company for $100,000 saying that we didn't pay him enough rent. That is of course not true. It's so easy for him to make false claims with the power and connections he has. The judge in the case has actually met with the landlord's attorney privately, outside of court. The judge has not done anything to him regarding his stealing the inventory that belonged to our U.S. Company. Now the furniture is dirty, damaged and broken. They threw in the trash $25,000 in hundreds of our logo items. He also stole our company files, so we don't have all of our papers to defend our company.

In the last 7 months I have repeatedly asked the Shanghai Foreign Investment office in Shanghai for help. After all, the U.S. allows them to bring Chinese Delegations to the U.S. and invite U.S. business people to invest in China. I did invest in China. They say they can't do anything to help me. I have brought it to the attention of the Chinese Consulate in Los Angeles and also the Director of the Shanghai Foreign Investment office in Los Angeles and he told me he is in LA and can't do anything about what happens in Shanghai. I never received any help from any of these offices about this matter.

I had notified the US Consulate in Shanghai immediately when this all happened. They had a gentleman from the Commercial section contact me. I was told there really wasn't anything they could do.

I received no help from anyone until Congressman Royce started looking into what has been happening and this hearing date was set. Then the action started happening. The Shanghai Foreign Investment office called me. They were looking for the U.S. Consulate to file a claim against the land lord. The gentleman at the U.S. Commercial section said they could not do anything without permission from Washington.

Mr. Huang who is the Director of the Shanghai Foreign Affairs had asked that I call him. Mr. Huang said it was "NOTHING," that my workers got pushed and shoved and threats put on their lives that they would be beaten.

The U.S. Consulate had a meeting with Mr. Huang. He said that he wanted to make a deal and he did not want me to testify. He said he could get a deal for me to pay the landlord $14,000 and he would forget the case. Mr. Huang said he asked the landlord if he stole the furniture and he said no. And Mr. Huang said he believed him. The furniture is in the landlord's warehouse and his own lawyer told the judge he took it all. There was no help on the part of the local Shanghai Government.

I hope that this will be a good lesson for other American Business people who are considering going to China. My story is one of thousands of cases that have happened to other American business people in China. I personally feel it has become a dangerous place to do business. There are so many greedy, well connected Chinese business guys in China that pay off the right people and get what they want and we have no recourse. You can see by my story how bad it can get.

I think that if the U.S. Consulate was able to respond immediately back in December when this happened and filed a complaint it would have been helpful. Waiting until 7 months later lost its impact.

I want to thank Congressman Royce and the other members of this committee for taking the time to hold this hearing and I hope that any American thinking of making an investment there will think twice. They are on their own in an unethical environment of payoffs and power where even the toughest of American business men and women have problems.

Mr. SHERMAN. I want to thank you for your testimony. It concerns me that Mr. Nelson has had to leave. Is there someone else?

Mr. ROYCE. I concur.

Mr. SHERMAN. Is there someone else here at a high level from the International Finance and Development folks at the State Department?

[No response.]

Mr. SHERMAN. Well, I believe we have this on tape; and I look forward to our staff visiting with Mr. Nelson and showing him this tape; and making sure that he reads the accompanying material, as well. It is a shame he and his chief assistants are not here; but he needs to hear this. Let us go on to Ms. Bianco.

STATEMENT OF MS. JONNA BIANCO, PRESIDENT, AMERICAN BONDHOLDERS FOUNDATION, LLC

Ms. BIANCO. Mr. Chairman, Ranking Member Royce, members of the committee, it is an honor for me to appear before you today to discuss a matter that merits your urgent attention; namely, the People's Republic of China's failure to honor its sovereign debt obligations and the impact of that failure on thousands of hard working American citizens and their families who own defaulted Chinese Government bonds.

As President of the American Bondholder Foundation, during the past 8 years, I have experienced enormous frustration from our efforts to secure the Chinese Government's repayment of sovereign debt obligations that the pre-Communist government sold to thousands of American bondholders across this country.

No less outrageous has been the failure of the United States Government to live up to its responsibilities to its citizens, to hold China accountable for its brazen repudiation of billions of dollars in sovereign bond-related debt.

The ABF was created in 2001, only after officials at the Department of State, the Department of the Treasury, and the National Security Council advised that the U.S. Government would not take

an active role in pursuing the settlement of China's sovereign default.

While sympathetic to the plight of American bond holders, these officials maintained that the bond default was a private citizens matter, and that there were more important policy priorities for the United States to pursue with Beijing; rather than asserting the leadership that the American people are entitled to from their government.

These officials declined to take an active role on behalf of the U.S. Government; recommending instead that I work with the Foreign Bondholders Protective Council, a non-governmental entity, to seek redress from the People's Republic of China.

Subsequently, I created the American Bondholders Foundation, and I identified and contacted individuals throughout the United States who hold defaulted Chinese Government bonds. Today, the ABF represents more than 15,000 American citizens, who hold unpaid Chinese bonds, from all walks of life and backgrounds.

The ABF also speaks on behalf of fellow bondholders from foreign nations, including Israel, Spain, Portugal, Belgium, France, Australia, and New Zealand.

I am delighted to report to you that many bondholders are with us in this hearing room today. I ask that if you are a bondholder, please raise your hand or stand.

They represent the thousands of families who have waited decades for their investments to be honored by the Chinese Government. Their stories are true financial hardships, endured as a direct result of China refusing to pay its debts, and indirectly by the failure of the United States Government to enforce the current laws and hold China accountable for its financial obligations. They are waiting for justice.

While the PRC refused to honor its obligation to pay U.S. citizens who own the defaulted sovereign bonds, they acknowledged the debt in 1987, when the PRC settled British claims on the same bond as those held by American citizens.

In that case, however, the PRC agreed to negotiate a settlement only after the British Government stood up to protect its citizens, and enacted a law denying China access to London's capital markets, as long as these sovereign defaults remain outstanding.

More recently, Beijing has also approached the French Government concerning settlement terms for French bondholders, after France filed a claim before the World Trade Organization seeking redress.

Clearly, the action to getting the PRC to the negotiating table required Federal Government intervention. Unfortunately, our repeated efforts to persuade the administration to speak on behalf of the ABF have been unsuccessful.

The ABF has also taken its case to the Securities and Exchange Commission, as we believe the PRC is sensitive to any questions concerning its credit worthiness.

We have petitioned the SEC on numerous occasions to enforce the law, by insisting on disclosure of material risk information concerning China's selective default to perspective American investors in future Chinese sovereign bonds, as well as in the debt and eq-

uity offerings of Chinese state-owned or controlled enterprises in our capital markets.

To date, the SEC has declined to take any action. As a result, potential American investors considering whether to purchase official Chinese financial instruments are kept in the dark about China's long-standing sovereign debt default and the risks associated with such an investment.

History has, after all, a tendency to repeat itself. The Chinese Government has, in the past, defaulted more than once on financial instruments to its investors. What prevents it from defaulting again?

Yet, the credit rating agency still assigned China an impeccable credit rating status. If American citizens or businesses default on their debts, it is reflected in their credit ratings. Why should China be held to a different standard and be permitted to mislead American investors?

Fortunately, several courageous members of the House and the Senate have, on a bipartisan basis, taken up the cause of these American bondholders. They have respectively introduced House Resolution 1179 and Senate Concurrent Resolution 78, calling on the SEC to address the issue of the Chinese selective default.

I would ask, Mr. Chairman, that copies of these resolutions, along with my written testimony, be made a part of the permanent record of this hearing.

Mr. SHERMAN. Without objection, so ordered.

Ms. BIANCO. Thank you, sir.

The ABF believes that the SEC has a solemn responsibility to ensure that such compelling risk related information is treated as material, and included in future prospectuses and filings with respect to Chinese Government and state-owned enterprises' capital raising efforts in the United States capital markets.

More egregious than the failure of the SEC to perform such function has been the behavior of the nationally recognized statistical rating organizations and our SROs. Entities that submit their criteria for authorization and acceptance as an official NRSRO. In violation of their own metrics and standards, these firms, including Moody's, Standard & Poor's, and Fitch have ignored China's official and selective repudiation of its debt to American bond holders. They continue to rate Chinese sovereign debt obligations and other offerings among the highest ratings. This selective inattention by the NRSROs smacks at the conflicted environment surrounding the sub-prime mortgage debacle and cries out for close congressional oversight. The potential consequences of the U.S. Government's continued inaction initially guard could prove debilitating for untold numbers of Americans currently investing in Chinese instruments.

Mr. Chairman, we have seen the eyes, if Members of Congress and their staff glaze over when they hear that we have been pressing for justice on these debt obligations for some 8 years. Many have failed to appreciate the fact that real hardworking American taxpayers trying to make ends meet are the victims of this callous Chinese Government betrayal of investor trust and legal standing.

In closing, I urge the members of this committee and the United States Congress, as a whole, to recognize and act on this blatant

injustice to innocent American investors and families. China has gotten away with flaunting the rules of the WTO and international trading and financial communities more broadly for some long, that it has been emboldened by this country's major market players, the executive branch, many in the Congress, the NRSROs, and even the SEC, to believe it can default with impunity on its sovereign debt to these good and decent Americans. Please use this occasion to serve notice on the Government of China that such behavior will no longer be tolerated. Lend your support to H. Res. 1179 and, thereby, encourage the SEC to recognize that China's outstanding sovereign debt default is material information that Chinese state-owned and controlled enterprises must disclose in their SEC filings. If the SEC acts to ensure that the rating agencies no longer can conceal such material facts on the investing public, it will not only help rectify a wrong done to the effected American bond holders, it will be restore integrity to the bond rating's process, a step that in the aftermath of the sub-prime fiasco should be an urgent priority for Congress.

Mr. SHERMAN. Thank you.

Ms. BIANCO. Mr. Chairman, I appreciate the opportunity to share with you and your colleagues this outrageous situation and offer a practical near-term approach to addressing it.

Mr. SHERMAN. Thank you.

Ms. BIANCO. Thank you.

[The prepared statement of Ms. Bianco follows:]

PREPARED STATEMENT OF MS. JONNA BIANCO, PRESIDENT, AMERICAN BONDHOLDERS FOUNDATION, LLC

INTRODUCTION

Mr. Chairman, Ranking Member Royce, and distinguished members of the Subcommittee, thank you for the privilege of appearing before the Subcommittee on Terrorism, Nonproliferation, and Trade to discuss a matter that merits your urgent attention: China's failure to honor its sovereign debt obligations, and the impact of that failure on thousands of hard-working American citizens and their families who own defaulted Chinese government bonds. The Executive Branch has refused to hold China accountable for its obligations under these bonds, and therefore has failed to uphold the legal rights of our fellow citizens. Consequently, we have turned to Congress to redress this injustice and, with bipartisan support, have introduced resolutions in the House and Senate to call attention to China's unlawful conduct.

AMERICAN BONDHOLDERS FOUNDATION

I am the President of the American Bondholders Foundation ("ABF"), which represents the claims of approximately 15,000 American families who hold defaulted sovereign-backed bonds that were issued by pre-Communist governments of China. The ABF was created in 2001 after officials at the Department of State, the Department of the Treasury, and the National Security Council advised that the U.S. Government would not take an active role in promoting the settlement of China's bond defaults. While sympathetic to the plight of American bondholders, these officials maintained that the bond default was a "private citizen's matter" and that there were more important policy priorities for the United States to pursue with Beijing. They recommended that I work with the Foreign Bondholders Protective Council, a nongovernmental entity, to seek redress from the Chinese Government. Subsequently, I created the ABF and identified and contacted individuals throughout the United States who hold defaulted Chinese Government bonds, receiving their power of attorney for the settlement of these defaulted bonds.

It is essential for the Subcommittee to understand the human dimension of this international financial issue. The bondholders whom the ABF represents consist mostly of low to middle-income families, and many of the bonds held by these families have been passed down through generations. These bonds are held by individuals and working families—not by corporations, banks, or institutional investors.

Calculating the value of debt obligations in the same manner as the U.S. Department of the Treasury, the bonds held by our fellow American citizens represent a financial patrimony now worth approximately $260 billion. Ensuring that China meets its obligation to honor these bonds is therefore not only a matter of international justice; it implicates the financial well-being and future of thousands of Americans.

BRIEF HISTORY OF CHINA'S DEFAULT ON ITS SOVEREIGN DEBT OBLIGATIONS

Between 1900 and 1938, the Imperial and Nationalist governments of China, confronted by the need to raise capital to deal with dire domestic economic problems, issued tens of thousands of bearer bonds—valued at hundreds of millions of dollars—that were backed by the full faith and credit of the Chinese government. Most of the bonds held by American bondholders were issued between 1912 and 1938 and sold by international banks, primarily HSBC and Deutsche Bank. These bonds also were promoted and sold in the United States through U.S. securities dealers, listed on U.S. securities exchanges, advertised in U.S. newspapers, and quoted regularly in financial journals. The bonds were sold to investors in the United States, Japan, and Europe, including U.S. servicemen in World War II who were encouraged to come to the aid of our then-ally, China. The most prevalent among the defaulted bonds held by American bondholders are the 1913 Chinese Government 5% Percent Reorganization Gold Loan Bearer Bonds, which matured in 1960.

From 1913 until 1939, the Government of China serviced its financial obligations under the bonds. In 1939, however, as financial conditions deteriorated amid the Japanese occupation of China, the Chinese Government ceased payments, prompting the default of the bonds. The Chinese Government, however, pledged its intention to resume service on the debts when economic conditions permitted.[1]

After the Communist Chinese overthrew the Nationalist government in 1949 and established the People's Republic of China ("PRC"), the new Communist regime refused to recognize the international bond obligations of the governments it succeeded and failed to renew payments on outstanding debt incurred by predecessor Chinese governments. In 1955, the PRC formalized its position and issued a written statement that it could not repay bonds previously issued by "the Kuomintang reactionary Government."

In May 1979, as part of the U.S. Government's official recognition of the PRC as the sole government of China, the United States and the PRC entered into an Agreement Concerning the Settlement of Claims. The agreement provided compensation to U.S. persons who had suffered a taking of property by the Government of the PRC, but expressly did not encompass the debt obligations of the Chinese Government associated with bonds issued by predecessor regimes.[2] In February 1983, however, the Ministry of Foreign Affairs of the PRC issued an official *Aide Memoire* in which it formally and expressly repudiated its defaulted sovereign debt obligations, proclaiming that "the Chinese Government recognizes no debts incurred by the past reactionary Governments of China and has no obligation to repay them. It is a long-established principle of international law that odious debts are not to be succeeded to."[3]

CHINA'S 1987 SETTLEMENT WITH BRITISH BONDHOLDERS

A substantial amount of defaulted Chinese Government bonds were held by British citizens. As a result, in 1986, the British Government imposed legal restrictions barring China and any of its state-owned enterprises from issuing debt instruments in British capital markets because of the PRC's refusal to honor debts incurred by Chinese governments prior to the 1949 Communist Revolution.[4] In June 1987, the British Government reached an agreement with the PRC in which the PRC agreed to a settlement with British citizens holding the 1913 5% Reorganization Gold Loan bearer bonds—the same bond issue held by many American bondholders, including

[1] Letter from J. Brian Atwood, Assistant Secretary for Congressional Relations, U.S. Dept. of State, to the Hon Charles A. Vanik, Chairman, Subcommittee on Trade, Committee on Ways and Means, U.S. House of Representatives, Dec. 11, 1979 ("Atwood Letter").

[2] In a letter from the U.S. Department of State to Congress in December 1979, the State Department expressly noted that "the PRC has not repudiated the bonds. . . ." Atwood Letter, *supra* note 1. In April 1981, the U.S. Foreign Claims Settlement Commission determined that there was no record that the PRC had "affirmatively repudiated" the defaulted bonds. *In the Matter of the Claim of the Welthy Kiang Chen*, Claim No CN–2–015, Decision No. CN–2–066, entered as Proposed Decision on Oct. 17, 1979 and reaffirmed as Final Decision on April 1, 1981.

[3] U.S. Foreign Broadcast Information Service, China Daily Report, Feb. 9, 1983, at B–1.

[4] Yacik, *1841 Repudiation of Mississippi Bonds May Limit State's Issues in Foreign Markets*, The Bond Buyer, Sept. 16, 1986.

the ABF bondholders.[5] Thus, the PRC acknowledged its legal obligation to honor the bonds. At the same time, however, the PRC made a conscious decision to remain in selective, discriminatory default with respect to American and other non-British bondholders.

CHINA'S PERSISTENT AND FLAGRANT DEFAULT

It is incontrovertible that China is in default on its sovereign debt obligations to American bondholders. First, the bearer bond certificates held by American bondholders expressly state on their face that "[t]hese obligations are intended to be binding upon the Government of China *and any Successor Government*." (Emphasis added.) Second, it is well established, as a matter of international law, that a successor government is responsible for the payment of sovereign debt obligations of a predecessor government.[6] As a leading international jurist wrote in the 1920s, "[a] monarchy may be transformed into a republic or a republic into a monarchy; absolute principles may be substituted for constitutional, or the reverse; but, though the government changes, the nation remains, with rights and obligations unimpaired."[7] The Restatement (Third) of the Foreign Relations of the United States provides that "[a] state is responsible under international law for injury resulting from . . . (2) a repudiation or breach by the state of a contract with a national of another state (a) where the repudiation or breach is (i) discriminatory; or (ii) motivated by noncommercial considerations, and compensatory damages are not paid; or (b) where the foreign national is not given an adequate forum to determine his claim of repudiation or breach, or is not compensated for any repudiation or breach determined to have occurred."[8]

Third, China's refusal to honor its sovereign debt obligations violates its obligations as a member of the World Trade Organization—a membership that requires China to abide by accepted international legal norms and to accept the commercial and financial practices of the international trading and investment community. Fourth, as noted above, China affirmatively has conceded its debt obligations with respect to these bonds, and has entered into selective default status, by entering into the 1987 settlement with Britain regarding British holdings of defaulted bonds.[9] Fifth, the ABF has received reliable reports that the PRC has notified the Government of France that it intends to settle the claims of French citizens who hold the identical series of defaulted bonds held by American bondholders.

China's evasion of its responsibility to repay its sovereign debt obligations stands in sharp contrast to how comparable bond defaults recently have been resolved. In 1986, for example, the Government of the Soviet Union settled the claims of British citizens who were holders of pre-1917 Russian Government bonds. In 1996, the Government of Russia settled the claims of French citizens who were holders of defaulted pre-1917 Russian Government bonds.

It is therefore clear that China has affirmatively and brazenly chosen to be in selective default status with respect to American holders of defaulted Chinese bonds, in flagrant disregard of its international legal obligations and the economic consequences of its actions for the thousands of American citizens waiting for justice from Beijing.

---

[5] *China, Britain Settle Claims*, New York Times, June 8, 1987; *Historical Debts Accord Clears Way for China to Eurobonds*, Xinhua General Overseas News Service, June 5, 1987

[6] *See Restatement (Third) of the Foreign Relations Law of the United States*, § 712(2) (1986); Bederman, *Creditors Claims in International Law*, 34 Int'l Law. 235, 250 (Spring 2000); Pieter H. F. Bekker, *The Legal Status of Foreign Economic Interests in Occupied Iraq*, American Society of International Law (July 2003); *Great Britain* v. *Costa Rica (Tinoco Case)* (1923) (holding new Government of Costa Rica bound by concessions and bank notes given by Tinoco, the former dictator of Costa Rica, to British companies), *reprinted* in United Nations, *Reports of International Arbitral Awards* (2006).

[7] *Great Britain* v. *Costa Rica (Tinoco Case)* (1923), *reprinted in* United Nations, *Reports of International Arbitral Awards* (2006).

[8] Restatement (Third) of the Foreign Relations of the United States, § 712(2) (1986).

[9] A 1981 decision by the Foreign Claims Settlement Commission of the United States also supports the view that the PRC is in default on its sovereign bond obligations. In that decision, the Commission found that it did not have jurisdiction over a claim against the PRC concerning bonds issued by the Kuomintang Government, on the grounds that the PRC had not repudiated its debt obligations. *In the Matter of the Claim of the Welthy Kiang Chen*, Claim No CN–2–015, Decision No. CN–2–066, entered as Proposed Decision on Oct. 17, 1979 and reaffirmed as Final Decision on April 1, 1981. That changed in 1983, however, when the PRC formally repudiated its debt obligation on the bonds.

VIOLATION OF SEC DISCLOSURE REQUIREMENTS

In addition to violating international legal standards, China and numerous state-owned and controlled Chinese enterprises ("SOEs") are currently in violation of disclosure requirements under U.S. securities laws. Numerous Chinese SOEs participate in U.S. capital markets and constitute "issuers" under the Securities Act of 1933. *See* 15 U.S.C. § 78c(a)(8) (defining "issuer").[10] Under Rule 10b-5, they are therefore prohibited from making disclosures to current and potential investors in filings with the Securities and Exchange Commission ("SEC") that contain misstatements or omissions of material fact. *See* 17 C.F.R. § 240.10b-5. Under U.S. securities law, information is "material" if there is a substantial likelihood that a reasonable investor would find such information to be important in determining whether to purchase the applicable securities. See 17 C.F.R. § 230.405 (SEC Rule 405); id. § 240.12b-2 (SEC Rule 12b-2).

Because information about outstanding defaults by an issuer clearly would be important to a reasonable investor in deciding to whether to purchase a security from that issuer, China's selective repudiation of its sovereign debt to American bondholders is a material fact required to be disclosed in SEC filings by Chinese SOEs. By failing to acknowledge China's selective default status in SEC filings by Chinese SOEs, these filings therefore unlawfully contain omissions of material fact that are misleading to potential American investors. To correct these omissions, such filings must include a clear statement that the PRC has selectively repudiated the sovereign debt obligations included by predecessor Chinese governments, so that current and prospective American investors are on notice of the risks associated with investments in Chinese SOEs. American investors are entitled to know that the Chinese Government refuses to honor the sovereign full faith and credit obligations incurred by the established and internationally recognized governments of China preceding the Communist takeover in 1949. They are entitled to all information pertinent to an assessment of whether an investment in a Chinese SOE may be at risk. Yet the SEC filings by Chinese SOE's are devoid of any disclosure regarding China's selective debt repudiation regarding bonds issued by pre-Communist Chinese governments.

ARTIFICIALLY HIGH CREDIT RATINGS

Ignoring evidence to the contrary, and in the absence of SEC filings containing required disclosure of China's selective debt repudiation, the Nationally Recognized Statistical Rating Organizations ("NRSROs") consistently accord artificially high ratings to long-term foreign currency debt of the Chinese Government. Standard & Poor's and Fitch accord "A" ratings to Chinese long-term foreign currency debt, while Moody's accords an "A1" rating. Under the standards used by these same NRSROs, these ratings would be degraded if they took into account China's repudiation of its sovereign debt obligations and its selective default status. Standards & Poor's, for example, assigns an "SD" (Selective Default) rating to a debt obligor that has failed to pay one or more of its financial obligations when it came due, where Standards & Poor's determines that the obligor has selectively defaulted on a specific issue or class of obligations but will continue to meet payment obligations on other issues or classes of obligations in a timely manner. A "Selective Default" rating precisely describes the status of the Chinese Government concerning its selective default on government bonds held by American citizens.

---

[10] Chinese SOEs listed on the Euronex Securities Exchange of the New York Stock Exchange include Aluminum Corp. of China Ltd.; China Eastern Airlines Corp. Ltd.; China Life Insurance Co. Ltd.; China Mobile (Hong Kong) Ltd.; China Netcom Group Corp. (Hong Kong); China Petroleum & Chemical Corp.; China Southern Airlines Co. Ltd.; China Telecom Corp. Ltd.; China Unicom; Guangshen Railway Co. Ltd.; Huaneng Power International Inc.; Jilin Chemical Industrial Co., Ltd.; PetroChina Co., Ltd.; Semiconductor Manufacturing International Corp.; Sinopec Shanghai Petrochemical Co., Ltd.; Suntech Power Holdings Co., Ltd; and Yanzhou Coal Mining Co., Ltd.. Chinese SOEs listed on the NASDAQ Securities Exchange include Aluminum Corp. of China; American Dairy; ASAT Holdings; Asia Payment Systems; AsiaInfo Holdings; Alpha Spacecom; Baidu.Com., Inc.; Beijing Med-Pharm Corp.; Brilliance China; China Automotive Systems; China Eastern Airlines; China Energy Ventures Corp.; China Cable and Communications; China National Offshore Oil; China Energy Savings; China Techfaith Wireless; China Telecom; Chinadotcom; China Unicom; China Netco; Chindex; Comtech Group; Ctrip.com; China Yuchai International; Deswell Industries; International Display Works; INTAC International; 51 Job, Inc.; China Finance Online; KongZhong Corp; eLong; Linktone; Ninetowns Digital World; Nam Tai Electronics; Netease.com; Pacificnet Inc.; Radica Games; Sina Corp.; Shanda Interactive; Sinopec; Sohu.com; Sinovac Biotech; Target Media; Tiens Biotech; Tom Online; UTStarcom; Watchdata System; Webzen; and Qiao Xing Telephone.

THE U.S. GOVERNMENT'S INDIFFERENCE TO CHINA'S DEBT REPUDIATION

Despite the ABF's efforts, the U.S. Government has failed to pursue the issue of China's failure to honor its debt obligations to U.S. citizens in Washington's bilateral relations with Beijing. In 1979, the Department of State took the position that because China had not affirmatively repudiated its bond obligations, "the appropriate channel for seeking compensation remains the Foreign Bondholders Protective Council."[11] Notwithstanding China's subsequent and express repudiation of its debt obligations in 1983, however, the Department of State has still not elevated China's selective default status to a meaningful bilateral issue in U.S.-Chinese relations. Indeed, as recently as 2003, the Department of State continued to refer inquiries regarding China's defaulted payment of the bonds to the private, non-governmental Foreign Bondholders Protective Council.[12] The Department of the Treasury has expressed support in principle for American bondholders holding defaulted Chinese bonds, but has refrained from pursuing the issue with the Chinese Ministry of Finance.

Federal regulators have been equally feckless. In the last three years, the ABF repeatedly has petitioned the SEC to require disclosure of China's selective default status in filings with the agency, on the grounds that such information constitutes material risk information to which potential U.S. investors are entitled as a matter of law. Chinese SOEs continue to issue debt and equity offerings in U.S. capital markets. Yet the SEC refuses to take the necessary action to ensure that potential American investors in these offerings are apprised of China's longstanding default on its sovereign debt obligations.

CONGRESSIONAL RESOLUTIONS

The failure of the Executive Branch to protect the interests of American citizens injured by China's repudiation of its debt obligations requires Congress to take action. Now pending before the House of Representatives and the Senate are two nonbinding resolutions—H. Res. 1179 and S. Con. Res. 78—which highlight the issue of China's selective default and call for greater transparency by China and its SOEs in their SEC filings. Both resolutions express the sense of Congress that China and its government-owned and controlled enterprises should be required to disclose information about the selective default status of Chinese bonds in prospectuses and filings with the SEC.

These resolutions represent small but critical steps forward in the quest for justice on behalf of American bondholders. The artificially high credit ratings assigned by the NRSROs perpetuate the cycle of China's indifference to its sovereign debt responsibilities. They give China an incentive to avoid a negotiated settlement with U.S. citizens regarding China's default on sovereign bonds held by U.S. citizens. And they provide "cover" to the SEC to forego holding China more accountable in SEC filings by the Chinese Government and Chinese SOEs.

CONCLUSION

There is an adage in the law that "Justice delayed is justice denied." For the thousands of American citizens who are entitled to full and fair redemption of Chinese sovereign bonds, justice has been delayed far too long. We appreciate the Committee's attention to this important issue, and we urge the Committee's support for the pending resolutions.

Mr. SHERMAN. Mr. Tonelson?

STATEMENT OF MR. ALAN TONELSON, RESEARCH FELLOW, THE U.S. BUSINESS AND INDUSTRY COUNCIL, EDUCATIONAL FOUNDATION

Mr. TONELSON. Good morning, Mr. Chairman, Mr. Ranking Member, and members of the subcommittee. I am very grateful for the opportunity to testify here on behalf of the U.S. Business and Industry Council and the 1,550 member companies it represents on the effects of U.S. Government action to help U.S. companies and investors do business abroad profitably.

[11] Atwood Letter, *supra* note 1.

[12] Letter from W. Michael Meserve, Acting Director, Office of Chinese and Mongolian Affairs, U.S. Dept. of State, to Marvin Morris, Jr., Aug. 13, 2003.

USBIC has been advocating for U.S. domestic companies, not multinational companies, but companies that want to make their product here when fair and equitable business conditions dictate that. We have been representing these companies. They are mainly small and medium sized and family-held manufacturing companies since 1933. We represent exactly the types of companies that create the highway's jobs that generate the technological progress and also productivity gains that everybody now understands are central to genuine American prosperity and not the kind, all the bubblized prosperity that we have had recently.

At this point, I would note that one of our member organizations, the Polyurethane Foam Association, has submitted its own statement to this hearing and I would respectfully request that it be inserted in the record.

Mr. SHERMAN. Without objection, so ordered.

Mr. TONELSON. Thank you, so much. We represent well-run companies. If you are in manufacturing, if you have been in manufacturing for a long time, and these companies have been family-held, often by the same one for generations, you have to be well run. They have survived literally decades of U.S. trade policy failures, starting from the U.S. Government's rollover and play dead response, to Japanese and West European predatory trade practices, dating back to the 1970s and 1980s. They have also been able to withstand the disastrous transformation of U.S. trade policy and to U.S. off-shoring policy, a trade policy designed to speed the off-shoring of U.S. production and U.S. jobs.

And, in fact, if you want to know exactly why the U.S. Government was so enthusiastic about letting countries like China and Vietnam into the World Trade Organization well before they were ready to engage in lawful and equitable economic and commercial behavior, that is exactly why. These trade agreements have never been mainly about promoting U.S. exports there. There is not too much consumption power there. People are poor to what are called low income countries. It was all about encouraging the supply of the U.S. market from U.S. and other multinational companies, who set up shop there. That is what it was all about and that is what too much of our trade policy has been about for decades. And our companies that frequently supply position parts and components to larger multinationals have been primary victims of this trade policy.

Now, lots of our companies are simply too small and too inexperienced overseas to export themselves, although, as I mentioned, they do supply larger companies that do export. At the same time, they, also, do not export because they understand that so much of the business models, so many of the economic development strategies created by most other countries and most other companies overseas are keyed to reaching the U.S. market. To supply the U.S. market, they figure, Why shouldn't we do the same? After all, it is our home market. We should enjoy enormous home field advantages, but too often that is not the case at all.

Having said that, many of them do export robustly. Some of them actually invest overseas, too, and they need American officials, either stationed overseas or stationed here, to be forceful advocates and crackerjack problem solvers and too often, that is not

remotely the case. I would add also that ensuring that U.S. businesses, who are able to take advantage of every financially sensible sales opportunity, no matter where it is, is crucial to our prosperity and it is, in particular, crucial to maintaining a strong manufacturing base at home, not a strong U.S.-owned manufacturing base in a place like, for example, China.

It is well known that U.S. manufacturing has a big jobs problem. It is well known that U.S. manufacturing has a big trade deficit problem. What is much less well know and what needs to be much better known is the U.S. manufacturing, manufacturing at home, has a big output problem, too. Rates of output growth have been slowing dramatically. All of the capacity expansions have slowed to a near halt. And strangely enough, much of this feeble performance has taken place during a time when Washington has poured record stimulus into the American economy, by any measure, record peacetime stimulus. Yet, this very feeble performance persists. It is almost as if Washington is pressing that accelerator way down and the car is just chugging along and that stimulus, of course, is not sustainable over any serious period of time or whatever.

So, we definitely forceful and effective U.S. official advocacy of U.S. companies' interest overseas when they run into discriminatory treatment. In my written statement, I have discussed in some detail two case studies. I could provide many, many more. But, these are two that I thought were of special interest, because they illustrate two different categories of problems that our companies face.

The first set of problems has been countered by a Georgia-based manufacturer of precision parts for a wide variety of industrial and also consumer markets. They mainly supply U.S.-based customers, but overseas sales represent about 15 percent of total sales. They need to be able to export to China, because so much of the overall manufacturing of the products, whose parts they are actually part of, is done there now. Since the manufacturing has gone overseas, American suppliers have to go overseas. They have to go after them. It just makes sense. And, yet, they are faced with Chinese trade barriers and all other discriminatory practices that can add up to 50 percent to their bottom line costs, relative to the cost of their Chinese-based competitor. And this problem exists not only in China; this is a global problem.

When they go to the U.S. Government for help or when they are encouraged by U.S. officials, as they have been, go after that exciting China market, go after that exciting Indian market, that is where the gulf is. Ninety-five percent of the world's consumers live there after all. When they are told that and when they are offered assistance, there is an almost utter disconnect between the types of assistance that they are offered and the business realities they face on the ground, in particular, the completely artificial government-imposed cost disadvantages, from currency manipulation, from discriminatory valuated tax systems, and from subsidies for virtually everything, including subsidies for exporting, which, by the way, illegal according to the World Trade Organization. So, again, what Kason needs and what the U.S. Government can provide or has been willing to provide have almost nothing to do with each other whatever, almost nothing.

My second example pertains to the previously mentioned polyurethane foam makers. There are about 50 companies. They employ roughly 30,000 American workers. Kason, by the way, employs about 250; but, of course, it is only one company. The foam makers and, in fact, all of us, who are lucky enough to have seats, are sitting on flexible urethane and foam, almost certainly. So, it is a product that you find everywhere. They face many trade problems that are actually made in the USA, themselves. In particular, their main chemical raw materials, which are increasingly not made here, have a rather high tariff on them. They need very badly a tariff suspension. They have not gotten it. It is excruciatingly difficult to actually obtain these. And the U.S. Trade Representatives Office has told them, essentially, wait in line. Wait in line, by the way, is a phrase that many smaller U.S. companies here from U.S. Government agencies, when they see clear help. In fact, it is almost the only phrase that they hear, "Wait in line, we have got bigger fish to fry."

But, the foam makers, also, face a major foreign problem and let us look at China, because that is a major challenge for them. The foam makers have compiled very convincing photographic and other evidence, which has been included in their statement, strongly indicating that it has become routine in Chinese foam making to use chemicals that have been outlawed in this country for decades, because they deplete the ozone, because they cause cancer. But, they are routinely used, it appears, in China.

Now, one could say, well, we should simply inspect Chinese factories. We must do a much better job there. I do not know how many Chinese flexible polyurethane foam factories there are. I suspect there are quite a few. And I would submit to you that it is prohibitively expensive for the U.S. Government to be sending all these inspectors to monitor the safety practices of Chinese factors on an ongoing basis, because this industry, obviously, is not the only industry that faces problems like this.

Something else needs to be done and this leads me to an important conclusion that I hope that the Members of Congress seated here will take very seriously, as well as so many others, and that is that the fundamental situation that exists in trade policy from the prospective of small and medium-sized manufacturing companies, who are doing exactly the kinds of things our Government wants them to, to undergo sustainable prosperity, from their perspective, our situation is not that we have got this whiz bang, wonderful trade policy, but it is just not implemented so well and maybe there is some lazy bureaucrats over here and maybe there are some cockeyed priorities over there. The main problem is that the trade policy, itself, has been broken. So, of course, the kinds of agency specific and practice specific fixes that a lot of us have been talking about at this hearing would be very useful, but our manufacturers would respectfully ask that this bigger broken trade policy picture be continually kept in mind. Thank you, so much.

[The prepared statement of Mr. Tonelson follows:]

PREPARED STATEMENT OF MR. ALAN TONELSON, RESEARCH FELLOW, THE U.S. BUSINESS AND INDUSTRY COUNCIL, EDUCATIONAL FOUNDATION

Good morning, Mr. Chairman, Mr. Ranking Minority Member, and Members of the Subcommittee. I am very grateful for the opportunity to testify today on behalf

of the U.S. Business and Industry Council and the more than 1,500 member companies it represents on the effectiveness of government action to help U.S. companies and investors do business abroad.

USBIC has been advocating for family-owned and other privately held companies—mainly small and medium-sized manufacturers—since 1933. The organization has been especially concerned about U.S. trade policy for the last two and a half decades. Our members overwhelmingly are capital- and knowledge-intensive companies. Typically, they supply precision components for large, extremely advanced machinery systems ranging from motor vehicles to aircraft to machine tools to medical devices to telecommunications networks. As such, they generate the types of technological progress, productivity gains, and living-wage jobs central to America's economic success so far and its economic prospects. In addition, the advanced production and innovation capability they embody, and the workforce skill levels they foster are critical for maintaining the world-leading defense manufacturing base on which our national security rests.

Our companies have been so competitive that they have survived literally decades of major U.S. trade policy failures—from Washington's unwillingness to respond effectively to predatory Japanese and European practices to its fateful, disastrous decision in the late 1980s to transform U.S. trade policy largely into an exercise in promoting the offshoring of production and jobs. Increasingly, however, the cumulative effects of these failures have been grinding these companies down, and convincing their owners that they should get out while the getting's still reasonably good. They believe—and the record makes clear—that foreign government support for their competitors will continue to intensify, while their own government remains generally asleep at the switch

Smaller and medium-sized domestic manufacturers generally rely heavily on domestic sales. Lack of resources, experience, and international contacts tends to make investing in foreign countries or even exporting directly to them prohibitively expensive. They are simply not in a position to absorb the kinds of front-end costs and take the risks required to set up foreign sales networks and support them over the long-haul—an indispensable ingredient of overseas success. The prospect of dealing with regulatory difficulties, intellectual property theft, and outright corruption is also extremely intimidating—especially in countries with little or no tradition of rule of law.

Moreover, these companies rightly believe that the U.S. market in its own right is by far their most promising in economic terms due to high incomes. Numerous foreign enterprises and governments, they constantly observe, have keyed their business and economic development strategies toward selling to the United States. The case for American companies being similarly focused is that much stronger.

Yet no business owner worth their salt is going to overlook a financially sensible revenue possibility, and many smaller domestic manufacturers export robustly and work hard to increase their foreign sales. The dollar's recent weakness against the Euro and many other major currencies clearly have opened opportunities—and produced results—that would have been inconceivable just a few short years ago.

To be sure, few small and medium-sized manufacturers I speak with—whether members of USBIC or prospects—are looking at the weak dollar as a cure-all. They know that currency manipulation is only one of many types of predatory trade practices in which foreign governments engage. Moreover, the revaluations in China and to a lesser extent Japan have unfolded much more slowly—and are likely to fall short of the mark needed to restore their price competitiveness vis-a-vis these two enormous trading partners.

These manufacturers also are starting to recognize a major downside to the weak dollar—exploding prices for the fuels, metals, and other commodities they require, which have hammered at their margins. And they realize that once started, a weak-currency policy can be very difficult to stop, especially for a country with enormous external debts like the United States.

Yet export markets continue to be of significant interest to many of these businesses. In addition, developments in foreign markets can decisively affect them in another important way. Specifically, foreign government actions and policies—ranging from currency manipulation to discriminatory value-added tax systems to illegal subsidies to lax environmental and worker safety regulations—can have a make-or-break impact on their competitiveness in the U.S. market and in third-country markets. So, by extension, can the U.S. government's poor record of addressing them.

The damage done by these U.S. trade policy failures can be seen far beyond the ranks of the small and mediums-sized companies with which USBIC works most closely. As is well known, the U.S. manufacturing sector has suffered immense job loss and unprecedented wage stagnation, on top of running up enormous trade deficits over every significant recent time period one cares to examine. Less well known,

however, are several measures of domestic manufacturing's competitiveness that carry an even more worrisome message.

For example, from 1997 through 2006 (the latest data available), the import share of the domestic manufacturing market jumped from 19.46 percent to 27.70 percent. For many advanced manufacturing sectors, like semiconductors, turbines, machine tools, and construction equipment, the levels of import penetration are much higher and their growth much faster. These data make clear that even many U.S. "industries of the future" are fighting a losing battle in their own home market, where they should enjoy enormous natural advantages. The data also indicate that the United States is becoming a much less competitive site for such advanced manufacturing.

Further, from 1997 to 2007, although overall U.S. economic growth totaled nearly 67 percent before adjusting for inflation, manufacturing output expanded only 26.25 percent, Measured as value-added, manufacturing's annual growth rate has been in steady decline since 1977. Excluding the tech bubble of the 1990s, the annual growth rate of manufacturing capacity shows similar feebleness, and since 2000, capacity expansion has virtually halted. In other words, U.S. manufacturing has a major output problem in addition to a major employment problem.

The recent weakness of output is all the more disturbing considering how accommodating the policy environment has been for the economy. Even before the Federal Reserve's radical interest-rate cutting and the tax rebate-induced rebound in the federal budget deficit since last summer, interest rates remained at multi-decade lows for years after the last recession ended, money supply growth exploded, the federal budget balance experienced a record swing from surplus to deficit, and the dollar weakened considerably. Yet despite the greatest injection of peacetime stimulus ever provided in U.S. history, industrial output lagged and overall growth remained subpar. Washington was flooring the accelerator, but the car was only chugging along. Clearly, something has gone terribly wrong with the nation's engines of growth.

Thus to remain strong in export markets, and to prevent predatory foreign practices or simple policy and regulatory arbitrage from disadvantaging American firms in markets around the world, U.S. officials need to be forceful advocates and crackerjack problem solvers. Yet in the experience of USBIC member companies, both descriptions are wide of the mark. Indeed, Washington's efforts on their behalf appear to be woefully inadequate, as the following two representative examples should make clear.

Kason Industries of Shenandoah, Ga., is the world's leading manufacturer of commercial refrigeration door hardware and employs some 250 workers. Since its founding in 1926, this privately held company has expanded into hardware and accessories for food service equipment, truck bodies, material handling, and industrial fabrication, among other markets.

The owner of about 50 U.S. patents, Kason is typical of the untold numbers of smaller manufacturers that rely heavily on continuous innovation. Although Kason believes that the domestic U.S. market will remain by far its most important, foreign sales represent about 15 percent of the company's total sales. In addition, Kason has been forced to start sourcing some component parts from China largely because of the PRC's predatory economic practices.

Kason has been encouraged by the U.S. government to take fuller advantage of high economic growth rates in China and other emerging market countries, but finds that federal officials lack a basic understanding of business realities on the ground. In particular, they appear to be ignorant of how predatory foreign actions and policies can much more than offset whatever market research, networking, and regulatory compliance advice Washington can provide.

For example, Kason's experience with the China market and Chinese competitors includes patent infringement as well as Chinese policies that directly and significantly affect the company's bottom line—and thus its price competitiveness These include the effects of currency manipulation, subsidized steel costs for China-based rivals, and a 13 percent rebate of the country's value-added tax granted to fabricated steel products that are exported. (The full value-added tax, it must be noted, must be paid by Kason for all of its exports to China, thus artificially raising their prices in China.)

According to Kason executives, federal-level legislators they have met often sing the praises of emerging markets, but seemed completely unaware of the discriminatory effects produced by a combination of VAT systems in most of these markets combined with America's failure to reciprocate. In fact, Chinese competitors have told Kason that they could afford to offer their products to U.S.. customers at or below production costs because the VAT rebate provided their profit. Kason has also been courted by the U.S. Commercial Service, whose Atlanta, Ga. office has offered

to help the company make business connections abroad, conduct surveys, and satisfy regulatory requirements. But Kason has yet to hear about a program that can help the company overcome the bottom line costs imposed by currency manipulation, VAT rebates, and other subsidies.

Incidentally, China is far from the only country presenting VAT-related problems to American industry. Kason reports losing almost all of its Italy business because of that country's 19 percent VAT, and that Spain's 16 percent VAT has been a major impediment to its potentially important appliance production market. Although VAT rebates do not appear to be a problem because neither country competes with Kason in the U.S. market, their VATs plus the freight and fees exporters like Kason need to pay to sell into their markets give Italian and Spanish producers a big edge in hanging on to their domestic customers.

Legislation to remedy the VAT situation—which could be responsible for as much as half the U.S. merchandise trade deficit—was introduced in the House in 2007. But the Border Tax Equity Act (H.R. 2600) has garnered only a handful of supporters.

The members of the Polyurethane Foam Association face somewhat different problems, but Washington's response has been just as ineffective. These companies produce flexible polyurethane foam that is used primarily in cushioning material in upholstered furniture and mattresses, and they employ more than 30,000 American workers.

As the Association's submission for the record makes clear, many of the most helpful measures Washington could take on their behalf would mainly affect the conditions of American production. For example, because the suppliers of their principal chemical raw materials have not adequately maintained their U.S. manufacturing base, the flexible foam makers must increasingly rely on imported ingredients. The United States maintains a 6.5 percent tariff on these imports, but not on the finished foam product.

The Association has investigated the possibilities of winning a tariff suspension for these chemicals, but has been told by the U.S. Trade Representative's office to get at the end of a long line of similar requests. The Association has also sought to persuade Congress to pass the legislation ultimately needed for the suspension, but to date no progress has been made.

The Association has no way of knowing how import levels have changed in recent years as a result of their relatively high production costs. Flexible polyurethane foam products have not been granted their own category in official systems for classifying the economy, despite repeated requests to do so by the PFA. Yet the foam makers do know that between 2005 and 2007 alone, their domestic output has dropped from 1.7 billion pounds to 1.3 billion pounds. A major reason: Much of the production of foam-using furniture has shifted to locations such as China. Indeed, during the above two-year period, Commerce Department data show that annual imports of upholstered household furniture from the PRC jumped from $1.1 billion to $1.7 billion.

The relatively high cost of foam production in the United States, of course, has created big obstacles to efforts by the U.S. foam producers to take the obvious step of trying to supply the growing upholstered furniture production markets in China and other developing countries. But the foam-makers also face another substantial problem—these countries' failure to impose the same regulatory burdens on its own producers that are borne by producers in the United States and other high-income countries.

Thus, as the PFA's submission shows, evidence abounds that China and other developing country producers make much of their flexible polyurethane foam with Ozone Depleting Chemicals such as CFC–11, whose use has been subject to an excise tax in the United States since 1990. The tax is supposed to be imposed on importers of products using these materials as well, but little enforcement of this provision is evident.

Producers in China can realize another cost break by using suspected human carcinogens such as methylene chloride n their foam. This very low-cost substance has not been used in American flexible polyurethane foam production for nearly two decades. But what is known about Chinese production methods—as presented in the PFA submission—indicates that use of CFCs or methylene chloride is widespread. Moreover, adopting safer alternative production methods and purchasing the needed equipment would add another layer of cost to Chinese production, and reduce major inequities in the trade relationship.

Unfortunately, many of these are problems that the U.S. government is simply not structured to deal with effectively. The Internal Revenue Service can and should review its enforcement activities related to the ODC Excise Tax on both imports of flexible polyurethane foam itself and of finished goods containing such foam. Yet the

cost of continuously inspecting the vast Chinese and other developing country production complexes alone clearly would be prohibitive.

All of which leads to a fundamental conclusion I hope that subcommittee members, their colleagues in the House and Senate, and Executive Branch officials will take seriously. The companies whose experiences I have described here clearly would welcome more effective assistance from Washington on various discrete, specific problems they encounter in overseas markets.

Yet as they also make clear, this piecemeal approach simply will not be enough. As one of them has put it, "The underlying problem is not lack of government help to overcome bad policy. The problem is the policy, which has indiscriminately opened U.S. markets to countries that don't share our regulatory values and/or economic priorities, and whose governments protect and support their industrial bases far more than does America's.

So the companies USBIC represents—and doubtless many others—certainly appreciate the subcommittee's interest in improving the performance of government agencies tasked with advocacy and problem-solving for U.S. firms in foreign markets. But they are also fervently hoping for changes in America's broader international trade strategy.

Mr. SHERMAN. Thank you. Ms. Bianco?

Ms. BIANCO. Yes, sir.

Mr. SHERMAN. How many cents on the dollar do the British get?

Ms. BIANCO. That has been undetermined, because it is not known as to the total amount of bonds that was actually turned in. That has been held confidential by the British Government, as well as China. We are working on trying to get as much information on that as possible.

Mr. SHERMAN. So, you do not know in gross dollars how much China paid or in percentage how many cents on the dollar the bond holders got?

Ms. BIANCO. Correct, sir. We know that is was millions and millions and millions of dollars that Great Britain received. How that equated to the quantity of the bonds to be turned in, we do not know.

Mr. SHERMAN. Okay. Let me move on to the next. How do you compare bonds issued by these now defunct Chinese governments with those issued by the Tsar, the Sultan of the Ottoman Empire, and/or by the individual states that were in rebellion during the War Between the States?

Ms. BIANCO. I am glad you brought that up, Mr. Chairman. Actually, in 2002–2003, Russia has actually stepped to the plate and honored the pre-Tsarist era bonds and has paid several hundred millions of dollars to France.

Mr. SHERMAN. Any idea how many cents on the dollar the Russians paid?

Ms. BIANCO. I just know, sir, that they have released several hundred million dollars at this time.

Mr. SHERMAN. And do you have a way to distinguish these bonds here from the Confederate money and, more particularly, the bonds issued the states that were in rebellion? Those state governments continue to exist both before and after the Civil War and, yet, of course, those bonds were never paid. Do you have a legal argument that distinguishes the Confederacy from San Yetsin?

Ms. BIANCO. No, sir. We would be more than happy to get one for you, Mr. Chairman.

Mr. SHERMAN. I appreciate that. I do not know whether every former government's debt should be paid, but I do know that we should be half as good a government as the British. And to see

them get paid and us not get paid illustrates that we do not have as good a government as the one in London, at least on this issue.

Mr. Tonelson, your testimony illustrates a point with our tariff system and that is we may impose a tariff on a raw material, but not on a finished good that contains that raw material, the effect of which is to lose all the jobs. I will give you an example. We impose a tariff on raw shrimp. We do not impose a tariff on breaded and cooked shrimp, so that what we do is we lose both the shrimp creating jobs and the breading and cooking jobs. Has there been a move to say that if we put a tariff on a good, that that tariff also applies to a more complicated product that contains that good?

Mr. TONELSON. I have not heard of one. And you are absolutely right, this has been a major failure, but not only of the U.S. trade policymakers, who have certainly underperformed for way too long a time, but frankly it has also been in too many instances a failure of manufacturing groups that do want to maintain the strong base here. And I will give you one very important example of that and that concerns the enormous fight within manufacturing over the steel tariffs that President Bush imposed in March 2002. This was an extremely difficult issue for my organization to deal with, because we have been long time advocates of much tougher, much smarter trade policies. At the same time, many of our manufacturers were steel users and——

Mr. SHERMAN. So, you would be in a circumstance where if the steel comes in as steel, we impose a tariff. If it comes in as a German or Japanese car, zero tariff.

Mr. TONELSON. Exactly.

Mr. SHERMAN. The easiest thing to do, of course, is when you impose a tariff on steel, you impose a tariff on anything that contains a lot of steel. You would have some de minimus rules, I mean a little bit. But, to impose a tariff on 1,000 pounds of steel, but to impose a zero tariff on a car, at the same time, invites losing the automotive jobs, as well as the steel job.

Mr. TONELSON. Of course. And it led to a very successful divide-and-conquer campaign in the U.S. manufacturing community by foreign producers——

Mr. SHERMAN. Was there any effort to have a steel tariff that included the steel within or as a major component of products or did we acquiesce in the divide and conquer?

Mr. TONELSON. It was never raised, to my knowledge, in the U.S. Government circles and to my great regret, we did not realize this problem early enough either and we have learned a very important lesson from that.

Mr. SHERMAN. I would like to work with your organization and some of my colleagues on legislation that says if we have a tariff, it applies to—where the product is 10 percent of that one thing. I mean, obviously, we do not want to be looking for microns of steel in a plastic device. But, for us to—as you point out, not only does it discriminate against the steel users in the United States, it then creates a wedge between the steel users, on the one hand, the steel producers, on another, and leads to the unraveling politically of our trade policy.

Mr. TONELSON. Absolutely.

Mr. SHERMAN. I look forward to working with you on that. I look forward to working with Ms. Bianco—did I pronounce your name right?

Ms. BIANCO. Bianco.

Mr. SHERMAN. Bianco and looking at the resolution she cited. Last question for Ms. Weinstein. Seven months ago, obviously, this government was not doing everything it should. Are there particular steps that you want Members of Congress or the State Department to take, at this time, that they are not taking?

Ms. WEINSTEIN. Well, it would be very helpful if the U.S. Consulate in Shanghai would file this report or this claim, I should say, against the landlord, which should have been done actually back in December. And the Shanghai Foreign Investment Office asked me why haven't they done that and when I asked the Shanghai Consulate why they had not done that, they said they were not allowed to do that; they would have to get permission from here. And I said, well, the Chinese Government thinks you should be doing this.

Mr. SHERMAN. Well, who do they need to get permission from?

Ms. WEINSTEIN. I have no idea. They just said Washington.

Mr. SHERMAN. The legal department. I think that they will be hearing from Members of Congress. I hope that you can provide to us the relevant assistant secretary's name.

Ms. WEINSTEIN. Thank you.

Mr. SHERMAN. Thank you. I yield to our ranking member.

Mr. ROYCE. Yes, Ms. Weinstein. You heard the Department of State's testimony and I would like you to respond to any of the comments that were made there, that you feel you would like to.

Ms. WEINSTEIN. Well, I forgot the gentleman's name, who was sitting at the end, he mentioned that regarding the judicial system in China, more or less referred to it, that it was young and beginning. You know, China is not a mom and pop country. It is not a mom and pop organization. They know what they are doing. My gosh, they were able to have all of these trillions of dollars paid to them. They sure can set up a legal system where a judge is not paid off, a lawyer is not paid off, just because those people have power in that country. So, I think it is fairly simple to set up a real law system, as we know it.

Everything that they were talking about, I do not know, I have been going to China for 14 years, so I guess I would say that I am a real pioneer going to China. I faced a lot of problems there. I know the things that exist. I know what other Americans there are going through. And it does seem like a lot of people are afraid to report this to the U.S. Government, because they will get retaliation later when they go back to China to try to do business, because the Chinese Government says, well, you know, we are not going to give him this contract or that contract, look what they did while they were in the U.S.

I do not know all of these agencies. He talks about hundreds of agencies and thousands of experts that are here to help American people in China. I would like to know just one or two that I could talk to, because I have not seen any of those over 14 years. And when I met personally with my director of media and communication, when the two of us met with the American Consulate general

in Shanghai back in the middle of 2006, I asked him—I told him all of what was happening and how we could not even get electricity installed in the building and all these many problems and he suggested that I join the American Chamber of Commerce.

Mr. ROYCE. Well, I know three serious cases where Californians were strong armed. But, I was going to ask you, given your experience over those 14 years, do you believe that your experience in China was unusual or are you aware of American businesses encountering similar treatment?

Ms. WEINSTEIN. Yes, I do. I know that my case is probably one of the more severe cases. But just a few weeks ago, the American Consulate commercial section told me that there was another American company, who has a retail store there, and they encountered the same thing, where some thugs came in and told their employees that unless their boss, the American paid more rent to their boss, that they would be hurt on their way home from work. So, those people quit. These things happen every day.

Mr. ROYCE. Are there cases in Orange County or elsewhere that you——

Ms. WEINSTEIN. Yes. There is a couple, who live in New Port Beach, who make educational material. They joint ventured with a Chinese gentleman in southern China. They bought the machinery from someplace in Europe. They shipped that machinery to China, put it in this man's factory, went there, taught him how to use it, all the employees how to use it. They gave him—because they felt he was their partner—they gave him all of the material and all of their customer base. After they did all of that, he locked the door and said this is all mine; who are you? They went to the local court system and the judge says, oh, no, you have no right to any of this. This belongs to this man. So, they were out like $2 million or $3 million or $4 million.

Mr. ROYCE. I knew of literally dozens of cases where people have been fleeced. Three cases, four, including yours, where people were physically threatened. You testified that you have repeatedly asked the Shanghai Foreign Investment Office for help with your case. You mentioned that this organization brings Chinese delegations to the United States and invites U.S. businesses to invest in China. The entity, as you say, has a Los Angeles office, right? So, tell us about your interaction with this organization. In your testimony, you seem to suggest that maybe that entity should not be permitted to court U.S. investments in this country, given the trouble that many of our U.S. businesses fall into.

Ms. WEINSTEIN. Well, I know for a fact that the U.S. allows Chinese delegations to come to the U.S. and they visit major cities, like Boston or Los Angeles or other places, and they put on a dog and pony show. And they bring all these other Chinese firms there and they say, you know, come to China, invest in this, and here is this gentleman, you can work with him, and this Chinese gentleman, you can work with him. And, of course, the Americans are so hospitable, so we have usually the local mayors are there and so forth and everybody is welcoming these Chinese and there is a really nice happy situation.

And then Americans are going, wow, this looks like a great opportunity. You know, I could do business in China. So, they go

there and they do this and they invest. But, then, the same thing happens, when something happens to them, there is nobody around. You know, where was this whole group that was going to help them in China? They just disappeared.

So, I think that we should really—you know, if we allow these delegations to continue to come to the U.S. and put on their dog and pony shows to entice Americans to invest, then we should have someone like myself to say, okay, now, you have heard the good side; let me tell you the bad side.

Mr. ROYCE. Why do not you give us just a quick rundown from the beginning, in terms of how you 14 years ago began to get involved in this and maybe culminate with what happened when you asked the Shanghai Foreign Investment Office for help with your case, given the role that these entities played in helping secure investment in China?

Ms. WEINSTEIN. 14 years is a long time.

Mr. ROYCE. Well, let me retract that.

Ms. WEINSTEIN. I am not sure I can talk——

Mr. ROYCE. Let me suggest that you just summarize how you became interested in making an investment in China.

Ms. WEINSTEIN. Right. If you remember about 1993–1994, our economy was kind of like it is right now. In California, especially, people were losing their homes. There was an upside down mortgages. And being an interior designer and having my own company, people were not decorating their homes. I read a tiny little article, because nobody talked about China in those days, and there was only about a million foreigners even going to China in those days and I read a tiny little article that Asia and especially China was the hot spot to go in. So, my daughter, who was 16, and I took off for Hong Kong and Beijing, not on a tour, all by ourselves. When we got to Beijing, I remember looking out the window, looking at all the construction cranes—at that time, 70 percent of the world's construction cranes were in China—saw the tremendous growth.

Looking around at their attempt at western design, which we would call American design, they referred to it as western design, I went, oh, my God, these people need my help, and I saw such an opportunity. And, you know, generally, the Chinese people are just very, very nice people and they were very helpful to me. And when I would show them my design work, they would go, oh, wow, this is really great.

And so, I went back to the U.S. and there was this gigantic magnet hauling me to China and I just, you know, thought, well, I need to be there. So, I went to Hong Kong more often at the beginning, because in those days, everything that was happening in mainland China was happening from Hong Kong. I did not actually know who I should meet; I just tried to do a lot of networking. I eventually met people in mainland China. I met the lady, who was vice president of China aviation and she gave me the opportunity to do the interior design of one of their most major hotels. We are all very good friends today and I have been a design consultant for that.

That kind of led me into more opportunities. I would go—you know, if I had 10 meetings, sometimes 10 out of 10, nothing hap-

pened; 9 times out of 10, it meant nothing. So, I spent a tremendous amount of my own money over these 14 years. I think I bought an airplane by now on United. And I have seen China grow. And all of those years, when I would go way back into the hillsides and look at factories, I did that alone, with no one with me. Getting off a plane, some guy with my name on a sign, going with him off into a parking lot to this tiny little village and driving for 2 or 3 hours back into the mountains. I was never afraid.

I would never do that today. China today is a different climate. The last time I did that, I took a bodyguard with me and even he said, oh, my gosh, you should never do that again today, because there were thugs on the highway. They see an American, they pull over the van, they take your money or whatever. So, it is a different climate. I have had many Chinese say to me, it used to be that you could pay someone off by giving them a case of cigarettes. Today, they want a Mercedes.

The greed has gotten tremendous in China and it is not a friendly situation, and I think because they think we are easy prey. Exactly what you gentlemen have said here today, the United States Government is doing nothing. It is like are we afraid to open our mouth that we might hurt their feelings? I mean, it is like, hey, we are real people. We are a real country. You know, we make real investments. Mine was $3 million just in the last 3 years. Another several million I have spent over the last 14 years trying to create a business and then created it, which you can see here, only to be destroyed with this local mafia kind of person. And all that furniture that you see sitting there, that was all made in the U.S. All of those sofas and chairs are made in the U.S. that I exported from here to go to China. And I do not know, it is really discouraging when I hear those two gentlemen, who were sitting here before us, talking about all of these agencies and all of these experts. Where are they? They are sitting down the hallways here, because they are not in China. And the one gentleman came over, shook my hand, and said, you know, I understand that our Consulate in Shanghai has been helping you. No, they have not. And he said, well, I understand we have made a lot of calls to you. No, they did not make any calls to me. I initiated about 20 calls to them and every time I would tell them an update of what was happening, the end of the conversation was, well, okay, Nancy, well, anything else that happens, let us know. Well, you are in Shanghai, what are you doing to help me.

So, I really feel that, you know, I am not Boeing. I am not General Motors. I am not Coca Cola. I am an American businesswoman, a very small grain of sand on the beach and no one paid any attention, because I am nobody. But, thank God, for Congressman Royce did pay attention and said, you know what, this is not acceptable and Chairman Sherman here, because you two have made a difference. I, hopefully, this will be the first step in the right direction for tiny small companies like myself.

Mr. ROYCE. Well, I want to thank you, very, very much, Nancy. I want to express my shock that the Department of Commerce and Department of State did not stay here to hear your testimony. And I thank the chairman, again, and I look forward to working with

him on the issues uncovered in this hearing. And I thank the other witnesses, too, for appearing today.

Ms. WEINSTEIN. May I say one more thing, is that this case is in China court right now, that the landlord is suing my China company for $100,000. The fact that the director, the Shanghai Foreign Affairs Office sits there and tells the U.S. Consulate people, oh, no, he did not steal her furniture. That pictures it he landlord's warehouse. That furniture was originally looking like that sitting in my showroom. For 2 weeks, we had wrapped everything, because we were trying to move it out to get away from him. That is the only reason it was even wrapped. I mean, it looks like you could just set a match to it now.

Mr. SHERMAN. I want to thank you and I am shocked that the Shanghai Consulate has not taken—just filed the paper that you asked them to file. And I would want to join perhaps with ranking member Royce in going to our chairman and pointing out that yesterday, we passed a bill through committee that is designed to provide equalization pay, call it special pay, for certain Foreign Service officers and I do not think that bill should come to the floor of the House until our Foreign Service officers in Shanghai do this one thing. If that holds it up a month, if that holds it up until next year, I hope not, because I would hope that that paper would be filed by the end of next week. So, I, for one, would be willing to vote against—and I support the bill. I voted for—well, I support the bill.

Mr. ROYCE. I think we just hold it.

Mr. SHERMAN. Yes, we just hold that bill until the State Department acts on this. So, let us hear from the gentleman from Arkansas.

Mr. BOOZMAN. Thank you. Mr. Tonelson, you represent a lot of different companies, I assume. Some of them have not done very well; fighting the battle that you suggest, some of them have done very well. I guess what I would like to know is what the difference is between the two groups. Where are you hearing the problems? Is it patent infringement? Is it being at the wrong place for the product? Going in naively? Tell me the difference between those two groups.

Mr. TONELSON. Okay. There are many, many problems that these 1,550 companies and many others that I work with, also, because we are always trying to recruit companies. There are quite a few of our member companies, who have run into problems, because they have been supplying the American automotive sector, which is obviously in deep trouble. At the same time——

Mr. BOOZMAN. In trouble, in the sense I need to find a different market or——

Mr. TONELSON. Well, perhaps; if you will let me continue. Not all of the American locator automotive sector is in equally deep trouble. There are foreign transplant operations here. A number of them were doing quite well, a lot better than the big three U.S. brand makers for quite some time until very, very recently.

I have heard so many companies say, you know, we would love to sell our stuff to Toyota, to BMW in South Carolina, to Mercedes in Alabama. They are not interested and that is because so many of these companies have brought over such enormous chunks or

links of their supply chains over to the United States. So, U.S.-owned companies located here often do not have the option.

Now, that has been changing at various paces, depending on product categories. What is interesting is that the real value in any motor vehicle is the drive train. It is the engine. It is the transmission, the gear box. That is where you make money. Most of that production remains in Germany, Japan, and South Korea. That has been a tough market to crack.

Now, in fact, many of these companies have said, you know, since the U.S.-owned Detroit automakers have not been doing so well and they may be doing a lot worse for the foreseeable future, since we cannot sell to the foreign transplants, we need other markets. They love the medical equipment market, which has been a very good market, and I would say that many companies that have managed to make that transition have achieved rather good success. There is something very important we have to remember, though, about medical equipment. That is that it is really very misleading to talk about the U.S. healthcare industry today as being private sector. It is very heavily subsidized. I do not know how much longer that can continue, because it is, as you well know, awfully expensive. But for now, it is working.

But, the most common complaint that I hear across industry ranges from companies that are not making it is that I have to compete against a Chinese rival that is able to sell the finished product at my raw materials cost. Yike. And it is not because the Chinese rival is so much smarter than his American counterpart. It is because the Chinese rival benefits from a 40 percent currency subsidy, a 15 to 20 percent value added tax rebate when you export. That is an export subsidy. That is not supposed to be legal. They benefit from land subsidies, from water subsidies, from fuel subsidies. You name it, in China, it gets subsidized if you export, especially to the U.S. market.

So, that is the big, big fight that they face and it is very frustrating for them to be told, well, you have got to innovate. And the reason is, when your margins have been destroyed by this cutthroat predatory government-created Chinese competition, where is your reinvestable capital? What are you supposed to use for money when you go out to buy machines, new equipment, et cetera? It is not there.

Mr. BOOZMAN. Well, it is all over, though, too.

Mr. TONELSON. Sorry?

Mr. BOOZMAN. I said, it is all over, too, in the sense—you mentioned the auto industry and the competition there is the Japans and the Germanys and the French, with those components. So, the problem is, what do you do about it? Does your organization or are you advocating high tariffs across the board?

Mr. TONELSON. I will tell you. We have advocated high tariffs across the board, except where a U.S. source of supply simply is not available. We are not happy about advocating that. We wish we did not think that was necessary. But, we firmly believe that this country is in such a deep hole, not only economically, but in terms of our international finances and you know how many trillions of dollars of net debt this country has run up in the last 5 years alone

simply because our trade deficits were so enormous, which means that our entire economic course is completely unsustainable.

We wish we did not have to recommend this. There are other measures we feel that can be very usefully taken, also. But, if anybody has got a much better idea, if anybody can suggest something else that has not already failed, please let us know. Why are you keeping it a secret?

Mr. BOOZMAN. Let me just finish, Mr. Chairman. I think you made a valid point earlier about the—you brought up the steel industry. And I had a business that—of course, if steel were one of your clients, then they would feel like, you know, that we needed the tariff, because they were in trouble at that point. And as a national security interest, a lot of people felt like we needed to protect our steel industry.

Mr. SHERMAN. Right.

Mr. BOOZMAN. I had a company that makes small engines and does tremendous. They sell all over the world. They sell all over the United States. They have a little niche in doing that. But, they came to me and said, "We have this tariff. If I buy the steel and my guy makes the handle for these things, it is much more expensive than buying the handle from overseas. I really like my guy that does it." So, you have the loss of jobs. On the other hand, like I say, if you are the steel industry, you have a whole different attitude about it.

Mr. TONELSON. Well, in fact, we——

Mr. BOOZMAN. So, it is particular and very difficult.

Mr. TONELSON. We represent both ends and here is how——

Mr. BOOZMAN. My manufacturer, though—let me finish—my manufacturer of the handles that went with the equipment—it was just a secondary deal—when you get down and press them, though, most of them feel despite the problems that we have got, that you create more problems with the tariff game than you do without, when you poll them individually.

Mr. TONELSON. Okay. I——

Mr. BOOZMAN. Unless you are talking about their specific industry.

Mr. TONELSON. If I may, let me respond in two ways. First of all to point out, we face this exact problem, because we represent steelmakers and steel users. So, what we did was we apply what we call a national interest test to all of our policy recommendations. We are not advocating for specific sectors. And we essentially told our steel users, we understand your frustration. We did not yet hit upon the idea of tariffing that final product, also. But, we told them, and here is what they were convinced by, we told them if this country allows its steel industry to be driven under by predatory foreign dumping, you may be next. In fact, you are likely to be next, because heavy subsidization and the consequent dumping is by no means restricted to the steel industry. It is increasingly the way business is done. It is increasingly the way manufacturing is done overseas. And if you have any doubt about that, check out the list of incredibly obscure products that have come up in terms of International Trade Commission antidumping cases. It is unbelievable, especially involving China. There is no need, it seems, in which they are not interested. So, again, I am glad that your en-

gine parts manufacturer has been prospering. But, I suspect he may be in the Chinese cross hairs before too long.

My second answer just involves the fact that whatever individual anecdotes one can tell, there is no doubt that U.S. domestic manufacturing, as a whole, is in deep trouble. And, again, if anybody else has any other idea that has not already failed, please let us know, on an economy-wide basis, not for niche products, because, boy, I would hate to see American manufacturing turned into a niche industry. That would be a disaster.

Mr. BOOZMAN. Thank you.

Mr. SHERMAN. I do have one idea and I hope you will work with Don Brodky of our committee staff on this and that is a law that says, if a product coming into the United States value added wise is 20 percent of a product on which we have a tariff, then we put the tariff on that product.

Mr. TONELSON. That is long overdue.

Mr. SHERMAN. I could imagine somebody just painting a happy face on a big plat of steel and saying, well, we are not importing steel, we not subject—it is a finished product. It is a work of art. It has a happy face. So, one can of spray paint should not be a disguise for a ton of steel and even turning that steel into a car should not necessarily disguise this ton of steel. We will work with you on drafting——

Mr. TONELSON. Please.

Mr. SHERMAN [continuing]. That legislation.

Mr. TONELSON. Thank you.

Mr. SHERMAN. One last thing, is there anybody here from the Department of State, who is still here taking notes? Good. We will want to arrange to make sure that the right people at State are seeing this transcript as soon as possible.

Is there anybody here from the Chinese Embassy? I see no hands for the record. We stand adjourn.

[Whereupon, at 12:20 p.m., the hearing was adjourned.]

APPENDIX

Material Submitted for the Hearing Record

9724 Kingston Pike, Suite 503
Knoxville, TN 37922
Telephone 865-690-4648
Fax 865-690-4649
E-mail rivedeka@pfa.org
www.pfa.org

Statement of the Polyurethane Foam Association
Filed with the United States House of Representatives
Committee on Foreign Affairs
July 17, 2008

This statement is presented by the Polyurethane Foam Association (PFA), a United States trade association whose members comprise manufacturers of flexible polyurethane foam (FPF) and suppliers of chemical raw materials and supporting technologies. PFA manufacturing members are predominately small businesses producing flexible polyurethane foam that is primarily used as cushioning material in upholstered furniture and mattresses. PFA manufacturing members produce more than 1.3 billion pounds of product each year and employ more than 40,000 Americans in production and foam fabrication facilities.

The FPF production industry is dependent upon demand from its customer industries. To be able to meet the requirements of upholstered furniture and mattress manufacturing companies and remain economically competitive, the United States FPF industry must be able to purchase chemical raw materials at parity with FPF manufacturers in other parts of the world.

The US foam industry's foreign trade concerns are not easy to solve. We face three difficult challenges:

1) Declining number of domestic raw material producers, combined with unnecessary tariffs on imported raw materials, drive customer industries offshore during periods of spot shortages of foam feedstock chemicals;

2) Customer industries shifting from domestic American manufacturing to increasing use of low cost labor Chinese upholstered furniture assembly plants;

3) Poor enforcement (or lack) of environmental and worker safety regulations in China and other developing Asian countries which allow manufacturers in those countries to operate with lower overhead costs and to use low cost chemical raw materials that are restricted or banned within the US.

Fast-Track Process Needed For Adjustments On Import Tariffs Applied To TDI And Polyol Chemicals.

Supplies of domestic chemical raw materials for FPF are declining. [1] The majority of US FPF chemical raw materials are supplied by global corporations such as BASF, Bayer, The Dow Chemical Company and Lyondell. These companies have been producing FPF raw materials for decades operating a handful of large United States chemical manufacturing facilities. Some of the older chemical manufacturing sites now require extensive maintenance and processing upgrades. In recent years, chemical industry publications have reported the closing of five US TDI manufacturing facilities,[2] leaving just four plants to supply the United States FPF industry. Scheduled maintenance, storms, and plant accidents can interrupt domestic TDI supplies.[3] While US TDI production capacity is declining, companies involved in global TDI supply are breaking ground on new high volume production facilities in China. News articles describe the new Chinese facilities as being able to operate at lower cost with greater throughput efficiencies. The picture is clear: the lure of a growing Chinese economy, combined with older US facilities that lack competitive production efficiency, are driving the US FPF supply chain offshore.

Ideally, a shortage of US raw materials could be offset by the availability of a competitive global supply. Unfortunately, restrictive tariffs on key FPF raw materials do not allow US manufacturers to shop the global market competitively.[4] We have been advised that obtaining a temporary tariff suspension is a lengthy and sometimes challenging legislative process. It would be beneficial to small American businesses to streamline the legal process for tariff initiatives or suspensions, allowing US tariff adjustments to occur in a timelier manner.

Creation of tax incentives rewarding research and development achievements particularly in the area of renewable resources and energy reductions in the production process would also help motivate global chemical suppliers to reinvest in America, upgrading production facilities and ramping up product research activities.

American Upholstered Furniture And Mattress Manufacturers Shift Production To Factories In China.

Fabric and filling materials such as FPF make up the highest percentage of manufacturing costs in a sofa. In the United States, the cost of assembly labor follows closely.[5] Because of storms, hurricanes, scheduled maintenance and accidents at domestic TDI plants, there have been a series of spot shortages in US foam supply to upholstered furniture manufacturers. These shortages, combined with across-the-board increases in furniture

---

[1] Polyol and toluene diisocyanate (TDI) are the two principal raw materials used to manufacture flexible polyurethane foam (FPF).

[2] In 2002, there were nine domestic TDI production plants located in Lake Charles, LA; Geismar, LA (3); Baytown, TX (2); New Martinsville, WV, and Freeport, TX(2) with a combined TDI production capacity of 1,723 million pounds. By 2008, plants in Lake Charles, LA; Geismar, LA (2); New Martinsville, WV and Freeport, TX had closed reducing total US domestic capacity to 982 million pounds.

[3] Lyondell Chemical permanently closed its TDI plant at Lake Charles, LA. in 2005 following damage caused by Hurricane Katrina. Closure of that plant eliminated 250 million pounds of domestic TDI capacity.

[4] Harmonized Tariff Schedule of the United States Supplement 1 (July 1, 2008) 2929.10.15 – 6.5% on imports

[5] An Update of Some U.S. Home Furnishing Trends; E.E. Reich, Journal of Cellular Plastics, Jan 1988; vol. 24: pp. 245 - 255.

component material costs, and available cheap labor are driving the manufacture of US upholstered furniture to China. According to the US Department of Commerce, the annual value of imported Chinese upholstered residential furniture grew from US $1.1 billion in 2005 to close to US $1.7 billion in 2007.[6] Over the same 2-year period, US FPF production volume dropped from about 1.7 billion pounds in 2005 to about 1.3 billion pounds in 2007.[7] Chinese furniture assembly provides an opportunity to produce long runs of nearly identical items efficiently, taking advantage of lower labor costs. Chinese furniture manufacturers are also able to purchase lower cost component materials. Maintaining strong US furniture manufacturing operations requires that component suppliers be able to provide materials at prices that are globally competitive. A temporary suspension of tariffs on key raw materials would help efforts to hold US manufacturing jobs.

Enforcement Of Existing US ODC Excise Tax Will Help Improve Environment And Achieve International Parity For Foam Products.

In 1989, Congress passed the Revenue Reconciliation Act. Section 7506 of the Act authorizes the Internal Revenue Service to enforce an excise tax to be applied to most manufacturers, producers, and importers of products that use of Ozone Depleting Chemicals (ODCs) in the production process.[8] The tax is imposed on any product imported into the United States in which an ODC was used as a material in its manufacture or production. Because of the type of production processes used in the manufacture of much of the flexible polyurethane foam produced in China, there is reason to believe that a portion of FPF manufactured in China is processed using CFC-11, a recognized ODC. Use of CFC blowing agents, or the suspected human carcinogen methylene chloride, would provide a significant cost advantage for Chinese manufacturers. CFCs have not been used in US FPF production for almost two decades. Methylene chloride also is no longer used in US foam production, and its use is highly restricted in all US manufacturing. Importers of Chinese upholstered furniture and mattress products containing flexible polyurethane foam which could have been manufactured with CFCs should be directed to comply with ODC Excise Tax requirements.

Exhibit A and B show the difference between typical manual "bucket" foam pouring practiced in China(Exhibit A) and typical continuous foam pouring technology(Exhibit B) as used in the United States. The Chinese "bucket" pouring process requires the use of either CFCs or methylene chloride, depending on the foam type. Adopting safer alternative methods would require the use of continuous pouring equipment and technology.

The Polyurethane Foam Association respectfully requests the committee to recommend initiatives to:

---

[6] US Department of Commerce reports, SIC 2512 (upholstered residential furniture), US Imports from China
[7] Polyurethane Foam Association Pounds Poured Reports (monthly census of PFA member production)
[8] The chemicals, primarily chlorofluorcarbons (CFCs), hydrochlorofluorocarbons (HCFCs) and halons, are listed in at 26 USC Sections 4681 and 4682.

1) Amend the tariff application process, allowing for timely temporary tariff adjustments to respond to critical market conditions, and to suspend the tariff applied to imported 2,4 and 2,6 TDI (2929.10.15) and polyether polyols (3907.20.00);

2) Offer incentives to businesses that demonstrate significant breakthroughs in environmental product improvements and / or major reductions in production energy consumption;

3) Direct the Internal Revenue Service to review monitoring and enforcement activities of the ODC Excise Tax that could be applied to importation of bulk flexible polyurethane foam and finished goods containing flexible polyurethane foam originating from countries known to use ozone depleting chemicals in their production processes.

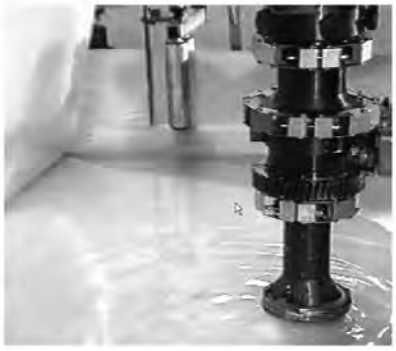
Sincerely,

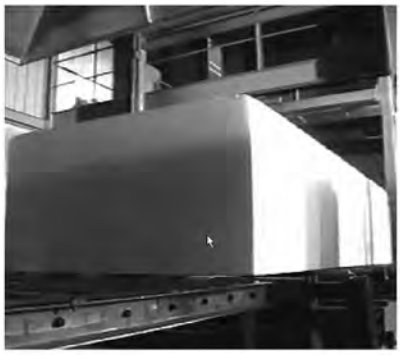
Robert J. Luedeka

Robert J. Luedeka
Executive Director

Exhibit A – Typical Manual Bucket Pouring as Practiced in China

Exhibit B – Continuous FPF Production





HRES 1179 IH

110th CONGRESS

2d Session

H. RES. 1179

Expressing the sense of the House of Representatives that the People's Republic of China and all enterprises owned or controlled by the People's Republic of China should make proper disclosures with the Securities and Exchange Commission regarding the selective default status of certain bonds.

IN THE HOUSE OF REPRESENTATIVES

May 7, 2008

Mr. GALLEGLY submitted the following resolution; which was referred to the Committee on Financial Services

RESOLUTION

Expressing the sense of the House of Representatives that the People's Republic of China and all enterprises owned or controlled by the People's Republic of China should make proper disclosures with the Securities and Exchange Commission regarding the selective default status of certain bonds.

Whereas sovereign debt obligations (in this resolution referred to as `bonds') of the Government of the People's Republic of China were offered and sold in the United States capital markets;

Whereas the bonds constitute full faith and credit sovereign obligations of the internationally recognized Government of the People's Republic of China;

Whereas the People's Republic of China subsequently defaulted on the bonds;

Whereas the United States Foreign Claims Settlement Commission determined that the bonds constitute an unpaid general obligation of the Government of the People's Republic of China;

Whereas under the successor government doctrine of settled international law (establishing the continuity of obligations among successor governments), the repayment obligation for the bonds is the obligation of the Government of the People's Republic of China;

Whereas the Government of the People's Republic of China has been duly notified by representatives of the affiliated United States creditors of the demand for repayment of the bonds;

Whereas the Government of the People's Republic of China continues to refuse to repay the bonds held by United States citizens and has officially repudiated the debts; a clear violation of United States law, international law, rules and regulations of the World Bank and the International Monetary Fund, and the United Nations Charter;

Whereas the Government of the People's Republic of China honored repayment of the bonds held by

British citizens while rejecting the claims of United States citizens;

Whereas the Government of the People's Republic of China, its state-owned enterprises, and other entities controlled by the People's Republic of China continue to enjoy open and unfettered access to the United States capital markets, while the Government of the People's Republic of China continues to reject the lawful claims of United States citizens;

Whereas the sales of securities in the United States capital markets issued by Chinese entities, including the Government of the People's Republic of China and its state-owned enterprises, fail to disclose both the existence of the defaulted debt of the Government of the People's Republic of China and the continued evasion of repayment of the bonds, the discriminatory treatment of United States citizens, and the People's Republic of China's repudiation of official debt;

Whereas the wrongful actions of the Government of the People's Republic of China are improperly concealed by the continuing publication of artificial `investment grade' sovereign credit rating classifications assigned to the Chinese Government by the 3 primary Nationally Recognized Statistical Rating Organizations (NRSROs) and this concealment fails to conform to the published definitions of those Organizations;

Whereas the continued publication of artificial `investment grade' sovereign credit rating classifications assigned to the Government of the People's Republic of China provides an incentive to the Chinese Government to avoid a negotiated settlement with United States citizens regarding China's default on its sovereign debt obligations;

Whereas the lack of transparency concerning the selective default of the Government of the People's Republic of China poses a material risk to the investing public and threatens the integrity of the United States capital markets; and

Whereas to provide relief to United States bondholders, restore transparency, uphold the rule of law, and affirm the validity of public debt contracts: Now, therefore, be it

> *Resolved,* That it is the sense of the House of Representatives that the People's Republic of China and its government-owned and controlled enterprises should be required to properly disclose material information concerning the selective default status of these bonds in all prospectuses and filings with the Securities and Exchange Commission.

SCON 78 IS

110th CONGRESS

2d Session

S. CON. RES. 78

Expressing the sense of Congress that the People's Republic of China and all enterprises owned or controlled by the People's Republic of China should make proper disclosures with the Securities and Exchange Commission regarding the selective default status of certain bonds.

IN THE SENATE OF THE UNITED STATES

April 28, 2008

Mr. INHOFE submitted the following concurrent resolution; which was referred to the Committee on Foreign Relations

---

CONCURRENT RESOLUTION

Expressing the sense of Congress that the People's Republic of China and all enterprises owned or controlled by the People's Republic of China should make proper disclosures with the Securities and Exchange Commission regarding the selective default status of certain bonds.

Whereas sovereign debt obligations (in this resolution referred to as `bonds') of the Government of the People's Republic of China were offered and sold in the United States capital markets;

Whereas the bonds constitute full faith and credit sovereign obligations of the internationally recognized Government of the People's Republic of China;

Whereas the People's Republic of China subsequently defaulted on the bonds;

Whereas the United States Foreign Claims Settlement Commission determined that the bonds constitute an unpaid general obligation of the Government of the People's Republic of China;

Whereas under the successor government doctrine of settled international law (establishing the continuity of obligations among successor governments), the repayment obligation for the bonds is the obligation of the Government of the People's Republic of China;

Whereas the Government of the People's Republic of China has been duly notified by representatives of the affiliated United States creditors of the demand for repayment of the bonds;

Whereas the Government of the People's Republic of China continues to refuse to repay the bonds held by United States citizens and has officially repudiated the debts; a clear violation of United States law, international law, rules and regulations of the World Bank and the International Monetary Fund, and the United Nations Charter;

Whereas the Government of the People's Republic of China honored repayment of the bonds held by

British citizens while rejecting the claims of United States citizens;

Whereas the Government of the People's Republic of China, its state-owned enterprises, and other entities controlled by the People's Republic of China continue to enjoy open and unfettered access to the United States capital markets, while the Government of the People's Republic of China continues to reject the lawful claims of United States citizens;

Whereas the sales of securities in the United States capital markets issued by Chinese entities, including the Government of the People's Republic of China and its state-owned enterprises, fail to disclose both the existence of the defaulted debt of the Government of the People's Republic of China and the continued evasion of repayment of the bonds, the discriminatory treatment of United States citizens, and the People's Republic of China's repudiation of official debt;

Whereas the wrongful actions of the Government of the People's Republic of China are improperly concealed by the continuing publication of artificial `investment grade' sovereign credit rating classifications assigned to the Chinese government by the 3 primary Nationally Recognized Statistical Rating Organizations (NRSROs) and this concealment fails to conform to the published definitions of those Organizations;

Whereas the continued publication of artificial `investment grade' sovereign credit rating classifications assigned to the Government of the People's Republic of China provides an incentive to the Chinese government to avoid a negotiated settlement with United States citizens regarding China's default on its sovereign debt obligations;

Whereas the lack of transparency concerning the selective default of the Government of the People's Republic of China poses a material risk to the investing public and threatens the integrity of the United States capital markets; and

Whereas to provide relief to United States bondholders, restore transparency, uphold the rule of law, and affirm the validity of public debt contracts: Now, therefore, be it

> *Resolved by the Senate (the House of Representatives concurring),* That it is the sense of Congress that the People's Republic of China and its government-owned and controlled enterprises should be required to properly disclose material information concerning the selective default status of these bonds in all prospectuses and filings with the Securities and Exchange Commission.

○